United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

74-2141

To be argued by
HERBERT M. WACHTELL

United States Court of Appeals

FOR THE SECOND CIRCUIT

D-Z INVESTMENT COMPANY,

Plaintiff-Appellee,

against

ROBERT E. HOLLOWAY, MELVIN S. TAUB, MAURICE J. BRICK, PETER E. SIMON, NORMAN BRASSLER, CHARLES GILLER, HERBERT E. HARPER, DR. GORDON McKINLEY, JAMES R. MOSELEY, III, JACK G. TAYLOR and DALLAS S. TOWNSEND, JR.,

Defendants-Appellants.

BRIEF ON BEHALF OF APPELLANTS

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BRIEF ON BEHALF OF APPELLANTS

Preliminary Statement

This is an appeal from an order of the Hon. Inzer B. Wyatt of the United States District Court, Southern District of New York, denying defendants-appellants' motion for a preliminary injunction upon their counterclaims charging violations of the federal securities laws by plaintiff-appellee.

This litigation arises out of an attempt by plaintiff-appellee D-Z Investment Company ("D-Z") to take over control of NJB Prime Investors ("NJB"), a real estate investment trust ("REIT") organized as a Massachusetts business trust. NJB is a public company the shares of which are traded on the American Stock Exchange (A356*). Defendants-appellants are the trustees of NJB. D-Z was incorporated in April 1974 by two Atlanta residents, Bruce R. Davis and Jerome Zimmerman, for the express purpose of acquiring control of NJB (A376-77). The total equity capitalization of D-Z is $10,000 (A435-36). It is this $10,000 investment which provides the sole equity base for D-Z's takeover bid for NJB, a listed company having outstanding 1,276,053 shares trading at the time D-Z commenced its takeover attempt at in excess of $7 per share—a total market value of $9,000,000 (Exh. C, A113, 115). From the outset, it was D-Z's plan to finance its takeover bid 100% by borrowings (Exh. G, A137; A227, 395-97, 825-28).

This action was originally commenced by D-Z on June 3, 1974—ten days prior to NJB's annual shareholders meeting. Shortly thereafter, D-Z—asserting supposed deficiencies in NJB's proxy materials—moved to enjoin the annual meeting or the voting of proxies in favor of the trustees. On June 11, D-Z's motion was denied in all

* References bearing the prefix letter "A" are to the Joint Appendix.

respects by Judge Cannella of the District Court (A20-25). On June 12, a further application by D-Z for injunctive relief in this Court was likewise denied (A76). The annual meeting proceeded as scheduled on June 13 (A358).

Thereafter, over strenuous objections by D-Z and those associated with it, intensive accelerated discovery was conducted by the trustees into the facts of D-Z's takeover attempt.* As will hereinafter be detailed in this brief, such discovery revealed that in this takeover bid, D-Z has engaged—and, unless enjoined, will continue to engage—in wholesale and flagrant violations of the federal securities laws. Accordingly, the trustees immediately moved in the court below for a preliminary injunction to restrain continuing illegal stock purchases and proxy solicitations by D-Z (A69-71). In support of that motion—by the testimony of D-Z's own witnesses and the documentary evidence from the files of D-Z itself as well as its "investment banker", Cantor, Fitzgerald & Co. (named as an additional defendant in the trustees' counterclaims)—the trustees showed to the District Court:

> that the Schedule 13D filed by D-Z upon becoming a 5% shareholder of NJB and all subsequent amendments thereto are unquestionably false and misleading in virtually every essential respect (see Point II, *infra*);
>
> that D-Z—in its attempt to finance through borrowings 100% of the price of its purchases of NJB shares (including D-Z's unregistered offer of its $1,250,000 issue of 6% promissory notes)—has been guilty of blatant violations of the margin regulations, the registration requirements of the Securities Act and the provisions of the Investment Company Act (see Point III, *infra*);
>
> that D-Z, through its "investment banker" Cantor, Fitzgerald—without benefit of any proxy filing as required by the proxy rules promulgated by the Securities and Exchange Commission—has engaged in a

---

* The trustees' attempts to obtain discovery were sought to be blocked by motions not only in the court below but in the Northern District of Georgia as well. Such motions were ultimately denied by Judge Duffy below and Judge Edenfeld in Georgia and the trustees' discovery proceeded on an urgent basis (A76-78, 173-74).

> telephone solicitation campaign of NJB shareholders seeking to array their support in joining with D-Z in a call for a special shareholders meeting for the purpose of ousting the trustees (see Point IV, *infra*); and
>
> that D-Z's large-scale purchases of NJB shares—both on and off the market—for the avowed and publicized purpose of obtaining control of NJB constitute in contemplation of law a "tender offer" in violation of the safeguards and requirements of the Williams Act (see Point V, *infra*).

After being twice adjourned upon request of D-Z,* the trustees' preliminary injunction motion ultimately came on to be heard before Judge Wyatt. By opinion and order dated August 23, 1974, Judge Wyatt denied the trustees' motion in all respects (A354-67). As to *each* of the grounds of illegality urged by the trustees, Judge Wyatt found no violation of law or even any "serious questions on the merits which amount to a 'fair ground for litigation'" (A366). As to a number of the grounds of illegality urged by the trustees, Judge Wyatt additionally ruled the trustees to be without standing (A361-62).

This appeal followed immediately. On August 28, 1974, upon application of the trustees, this Court ordered an expedited hearing of this appeal.

The District Judge who determined this motion adversely to appellants is able and experienced. Nonetheless, it is respectfully submitted that in rendering its decision, the District Court inexplicably committed major errors—both in essentially ignoring the uncontradicted record evidence before it and in adopting conclusions of law diametrically in conflict with controlling interpretations of the federal securities laws by this Court and the Supreme Court. Thus, by way of example only:

(1) The basic premise underlying the District Court's decision is its candidly expressed view that in struggles for corporate control such as in the case

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* As a condition of such adjournments, D-Z consented to a stay granting the trustees interim relief substantially as sought in the preliminary injunction motion itself.

at bar, "[m]anagement is simply trying to protect its entrenched position" and "while [the] attackers must obey the securities laws, enforcement of those laws is, with rare exceptions, best left to the SEC or to the stockholders of NJB [the target company]" (A361). In reaching this conclusion, the District Court flies in the face of the prior holding of this Court in *GAF Corp.* v. *Milstein**—a case which although strongly urged by the trustees below is not so much as cited in the District Court's opinion—unequivocally setting forth that in fights for corporate control the target company (precisely because of its "self-interest" as well as its resources) is the *best,* if not the *only* party in a position effectively to enforce compliance with the securities laws and to protect the public interest, and that such enforcement can *not* be left to either the SEC or the stockholders (see Point I, *infra*);

(2) With reference to the trustees' overwhelming showing that D-Z's Schedule 13D and the amendments thereto were egregiously false and misleading, the District Court in its opinion:

(a) first chose to take the view that the "basic argument" of the trustees "on this point depends entirely on their other argument * * * that D-Z had made a 'tender offer' " (A365) —which the District Court found it had not (A364)**; and

(b) then, in a single sentence, without discussion, explanation or findings of any facts, summarily concluded: "It is not shown that the Schedule 13D or any amendment is false or misleading" (A366).

In so doing, the District Court:

(a) surprisingly misstated the actual "basic argument" of the trustees that the issue of falsity of the Schedule 13Ds was in *no way* dependent upon the trustees' quite *separate* and *addi-*

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* 453 F.2d 709, 719-21 (2d Cir. 1971), *cert. denied,* 409 U.S. 910 (1972).

** The tender offer question is treated in Point V of this brief.

tional argument "that D-Z had made a 'tender offer' " and that—as expressly held by this Court in *GAF Corp.* v. *Milstein, supra,* as well as by other courts in any number of cases—the law was clear that an injunction would issue for a false and misleading Schedule 13D whether or not the company filing such Schedule was engaged in a tender offer (see pp. 19-26, *infra*); and

(b) chose to disregard the trustees' incontrovertible factual showing—from the mouths of D-Z's own witnesses and the evidence of D-Z's own documents—that D-Z's Schedule 13D and the amendments thereto were, indeed, unquestionably false and misleading in the most essential respects (see pp. 26-35, *infra*).

(3) The District Court in a single, conclusory sentence, without supporting findings or explanation, ruled that "no showing has been made of any violation of the margin requirements" (A361), notwithstanding:

(a) a detailed evidentiary showing by the trustees that the combined activities of D-Z and Cantor, Fitzgerald, a registered broker-dealer, in arranging for borrowings by D-Z of *100%* of the purchase price of shares of NJB, a listed company, constituted an unquestioned violation of the margin regulations (see pp. 41-46, *infra*); and

(b) that D-Z itself in its brief in the District Court, had not even *attempted* to justify the legality of its financing schemes under the margin regulations, but rather relied *solely* on a claim of supposed lack of "standing" in the trustees to raise the issue of illegality.

(4) The District Court, yet again in a single conclusory sentence, ruled that "no showing has been made of any violation of the 1940 Act or of the 1933 Act" (A361-62), notwithstanding:

(a) a detailed, overwhelming and uncontradicted evidentiary showing by the trustees that the unregistered offering by D-Z of its $1,250,000 issue of 6% promissory notes was—under controlling precedents of the Supreme Court and

the Courts of Appeals—an illegal public offering of securities in violation of the 1933 Securities Act (see pp. 46-52, *infra*);* and

(b) once again, that D-Z itself in its brief below did not even *attempt* to contest the trustees' showing of illegality, but rather sought to shield its violations of the 1933 and 1940 Acts from challenge *solely* by an argument that the trustees supposedly lacked "standing" to raise the issues.

(5) Finally, with respect to the trustees' showing that D-Z had engaged in an illegal proxy solicitation by telephoning NJB shareholders to seek their consents for the call of a special meeting of shareholders, the District Court in its opinion held the trustees' claim to be "without any support in fact" (A365). Somehow, the District Court reached this conclusion notwithstanding:

(a) the *admission* by a Cantor, Fitzgerald vice president that—acting on behalf of D-Z and pursuant to the instructions of his superior, and utilizing a summary schedule of block holders of NJB shares prepared from the NJB shareholders list—he placed telephone calls to more than the statutory minimum of NJB shareholders, asked the shareholder's position with respect to the call of a special meeting (he "might have" asked whether the shareholder was willing "to join in an effort to obtain a special meeting"), and then carefully noted on his schedule the results of such conversations, *e.g.*, "will not join in", "may give proxy", "will give proxy" (see pp. 53-56, *infra*); and

(b) that under controlling precedents of the Supreme Court and this Court—none of which are in any way alluded to in the District Court's opinion—as well as the express terms of the SEC's proxy rules, such telephone calls

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* Given the fact of such public offering—which rendered D-Z ineligible for a private company exemption under the 1940 Investment Company Act—it is undisputed that D-Z otherwise constituted an investment company required to be, but not, registered under the 1940 Act. See pp. 52-53, *infra*.

> indisputably constituted an illegal solicitation of a "proxy, consent or authorization" with respect to a listed security (see pp. 56-59, *infra*).

It should be noted that no live testimony was taken before the District Judge on the trustees' motion for a preliminary injunction (A355). Rather, the motion was decided exclusively on the basis of affidavits, transcripts of deposition testimony and documentary evidence submitted by the respective parties. Appellants are of course cognizant of the general doctrine that this Court will normally give deference to the discretion of the District Court in granting or denying a motion for a preliminary injunction. This doctrine, however, does not apply where, as here, there has been no live testimony and the record before the District Court consists exclusively of written evidence. As this Court recently recognized in *SEC* v. *Spectrum, Ltd.*, 489 F.2d 535, 540 (2d Cir. 1973)—reversing the denial of a preliminary injunction in a securities case—"we need give no special deference to the district court's finding * * * for 'we are in as good a position as [he] to read and interpret the pleadings, affidavits and depositions' ". *Accord, e.g., Dempster Bros. Inc.* v. *Buffalo Metal Container Corp.*, 352 F.2d 420, 423 (2d Cir. 1965); *Dopp* v. *Franklin National Bank*, 461 F.2d 873, 879 (2d Cir. 1972).

It is submitted that a review of the uncontroverted record herein must lead this Court to the conclusion that the District Court erred. As will hereinafter be detailed in this brief, D-Z has been engaged in wholesale violations of the federal securities laws and, under controlling principles of law, a preliminary injunction must issue.

Statement of Facts*

This takeover fight is the culmination of a plan conceived by two Atlanta entrepreneurs, Bruce R. Davis and Jerome Zimmerman (the "D" and the "Z" of plaintiff D-Z), aided

* Additional facts particularly germane to specific legal arguments are included at the appropriate point of discussion in the Points of this brief.

by the brokerage firm of Cantor, Fitzgerald, Inc. In or prior to early January 1974, Davis and Zimmerman—who had previously been joint promoters of at least one local Atlanta-based real estate syndication (A85-91)—discussed the concept of taking over control of a "public" real estate financial institution whose stock, due to prevailing market conditions, would be underpriced in comparison to the underlying book value of its assets (A377-79, 733-36).

Neither Davis nor Zimmerman had the financial wherewithal to finance the plan. The original discussions thus ended inconclusively (A386-89).

In January 1974, Davis then approached Cantor, Fitzgerald, a California-based brokerage firm having an office in New York, to ascertain whether that firm would act as an investment banker for Security Management Co., a company controlled by Davis, in obtaining an acquisition or merger candidate (A518-25). Cantor, Fitzgerald soon thereafter proposed two Florida-based companies as potential acquisition candidates (A531). Both of these prospects were abandoned in late February (A541-42).

Both Cantor, Fitzgerald and Davis continued to seek an acquisition candidate for Security (A542). In late February or early March, Davis came to New York and proposed to Cantor, Fitzgerald the idea of attempting to obtain control of a REIT (A542-45). Davis' thesis was that due to adverse market conditions, there were a large number of REITs having underlying asset values far in excess of the total market value of their outstanding stock (A377-79, 733-36).* Davis brought with him extensive information concerning the finances and operations of some 25 REITs, one of which was NJB (A542-43). The task of obtaining additional information was divided between Davis and Lawrence Orbe, a New York-based vice president of Cantor, Fitzgerald (A515-16, 548).

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* "I have made a careful study of various REITs which have a market value of between 40% to 60% of book value. * * * [I]t is my opinion that if a successful tender could be made for the shares of beneficial interest, you would be buying dollars for 40% to 60% of the dollar." (Exh. D, A222.)

Ultimately, Cantor, Fitzgerald narrowed the potential candidates to four: NJB was still on the list (A553-54). Finally, the list was narrowed to one: NJB.

During this period, Davis formulated his plan for NJB once control would be achieved. Specific properties of NJB would be sold (A554-58); the existing adviser would be removed to be replaced by Davis' own group; ultimately NJB's tax-exempt status would be abandoned; then NJB would be merged with Davis' own company and its assets used to pay off the debt that would have to be incurred in its acquisition (Exh. D, A221-24). Davis set forth his plans to Cantor, Fitzgerald (A46-60). Davis detailed his plans in writings to be used to attempt to raise financing for the takeover venture (Exh. D, A221-24; Exh. 25, A1747-50).*

In March 1974, Orbe of Cantor, Fitzgerald commenced to seek financing for Davis' takeover bid of NJB (A598-602). Orbe opened communication with an affiliate of CNA Financial Corporation (A144). CNA, as known to Orbe, was itself a holder of approximately 100,000 NJB shares (A599, 611). Meetings were arranged by Cantor, Fitzgerald to be held between the prospective co-venturers (A599-60). Initially, the negotiations proceeded smoothly: on March 21, 1974, a letter of intent was entered into between Davis and CNA's affiliate looking toward "the making of a tender offer for NJB Prime, a Massachusetts real estate investment trust." A new "tendering entity" would be formed to be owned "51% by the Bruce Davis interests". All monies used by the tendering entity would be borrowed. The bulk of the necessary financing would be provided by the CNA side of the venture, the NJB stock to be pledged to secure the loans. Control would be obtained over NJB. "The purpose of this control will be to vote to change the status of NJB from a REIT to an ordinary operating cor-

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* The takeover would be accomplished by a tender: "I propose that a surprise tender be made. * * * Initially, we would tender for a minimum of 51% of the shares of beneficial interest." (Exh. D, A222.)

poration." An ultimate combination of NJB, the "tendering entity" and Security would then take place. And "The result of this would be a transfer of the original debt used in the tender offer to NJB" (Exh. A, A108-09).

The next day a formal agreement for compensation was entered into between Davis and Cantor, Fitzgerald (Exh. 28, A1751-52). Cantor, Fitzgerald was to receive a percentage commission for any financing that it had assisted in arranging; Cantor, Fitzgerald was to receive separate compensation as Dealer-Manager on any tender offer; Cantor, Fitzgerald was to receive still further compensation "if we find an appropriate acquisition candidate" (Exh. 28, A1751-52). Cantor, Fitzgerald had been actively seeking such "appropriate acquisition candidate": During the period that negotiations were underway to secure CNA's financing for Davis' plan, Orbe of Cantor, Fitzgerald sought to make contact with key NJB personnel to attempt to enlist their cooperation in a "friendly" takeover (A606-08): Orbe's client was interested "in acquiring for cash 51% or more of the shares of beneficial interest of NJB Prime Investors" (Exh. B, A110).

The CNA-financed tender offer never reached fruition. Orbe's approach to NJB was rebuffed (A607-08). Shortly thereafter, CNA—faced with takeover problems of its own —withdrew from the venture (A628-29, 774).

Having lost CNA as the financial source for his takeover of NJB, Davis turned back to Zimmerman. Now Zimmerman was to raise the necessary funds (A388). The immediate plan would be more modest than a CNA-financed tender offer for 51% of NJB's stock. Rather, Zimmerman would raise $1,250,000; this amount would be joined with margin borrowings to create a $2,200,000 fund; this, it was calculated, would be sufficient to purchase 300,000 shares, or approximately 25% of NJB's outstanding stock (A388-96).

A new corporate vehicle for the takeover—D-Z Investment Company—was formed on April 23 to be owned

equally by Zimmerman and Davis' controlled company, Security. Zimmerman and Security each purchased 50 shares of D-Z's stock at $100 per share for a total equity investment of $10,000 (Exh. G, A132; A435). All other monies for the takeover of NJB would be borrowed (Exh. G, A137; A388-96). The express purpose for the formation of D-Z was to seek control of NJB (A377, 1279-81).

A new agreement was entered into with Cantor, Fitzgerald (Exh. 7, A1728-29). Cantor, Fitzgerald would "perform certain services". Cantor, Fitzgerald would be "exclusive purchasing agent" for all shares purchased. Cantor, Fitzgerald would be compensated: a $30,000 fee plus its expenses plus 5% of the net purchase price payable in respect of all such shares purchased. It would be Cantor, Fitzgerald's job to come up with the margin financing (Exh. 7, A1728-29).

D-Z authorized the issuance and sale of $1,250,000 in 6% promissory notes (Exh. G, A133). The notes were to be sold in 25 units of $50,000 each (A491-92). Zimmerman would solicit as many persons as were necessary to obtain purchasers for the notes (A505-08, 511). Zimmerman immediately commenced his efforts.* See, pp. 48-52, *infra*. And even before D-Z was actually incorporated, Davis—through Cantor, Fitzgerald—commenced purchasing NJB shares (A646, 651-52).

At the outset, the plan for seizing control of NJB appeared to be proceeding smoothly. Within only ten days after D-Z's incorporation, Zimmerman had been successful in raising $350,000 by sale of the 6% promissory notes (Exh. C, A120); Cantor, Fitzgerald came forward with $3 per share margin loans (Exh. C, A113); D-Z had acquired over 70,000 shares of NJB (Exh. C, A116).

Then difficulties arose. By mid-May, Zimmerman was finding himself unable to sell additional promissory notes (A512, 875-76). Davis and his associates, the brothers Ralph and Saul Becker, turned their efforts to attempting to borrow funds for D-Z by sale of the promissory notes or

* The particulars of D-Z's offering of its $1,250,000 note issue are detailed in Point III of this brief. See pp. 48-52, *infra*.

other means (A857-84). They sought funds in Miami Beach (A880), in Chicago (A880-84), in New York (A867-71). They were unsuccessful (A857-84).

The promoters therefore focused their attention upon the upcoming June 13 regular annual meeting of NJB shareholders. A copy of the NJB shareholders list was demanded and ultimately obtained (A1168). In late May, Georgeson & Co. was retained as proxy solicitors in anticipation of a proxy contest (Exh. 22, A1745). And only ten days before the scheduled date for the meeting, D-Z commenced this action in this Court seeking to block the meeting or the voting of proxies for the incumbent trustees (A4-19, 357). D-Z's attempts to obtain interlocutory injunctive relief were rebuffed by the District Court and this Court (A20-25, 76). The annual meeting went forward as scheduled (A358). The trustees were elected (A358).

That same afternoon of June 13, subsequent to the annual meeting, Davis and Becker of D-Z and Orbe and William F. Miller, a senior vice president of Cantor, Fitzgerald, met with their attorneys to plan their future course (A679-80). A new immediate goal was set: to obtain not less than 20% of NJB's shares—the amount necessary to call a special meeting at which an attempt would be made to obtain control of NJB (A677-80). Davis authorized Cantor, Fitzgerald to purchase unlimited quantities of NJB shares (A678-79, 683-84). At the same time, Davis and Cantor, Fitzgerald would intensify their efforts to come up with a major source of financing for D-Z which would permit D-Z to make a formal tender offer for NJB shares to obtain control (A779-821).

The very next day, Schwartz—another vice president of Cantor, Fitzgerald—acting upon instructions of Miller, proceeded to commence an intensive telephone campaign of block holders of NJB stock either to buy their shares or enlist their support in a call for a special meeting. See pp. 53-56, *infra*. Schwartz through these calls was successful in purchasing 5,000 shares (A1032-34). At the same time, Orbe of Cantor, Fitzgerald was actively buying NJB shares on behalf of D-Z on the American Exchange (Exh.

A, A208). By June 18, Miller instructed Schwartz to stop buying blocks. Schwartz was nonetheless to continue his calls to shareholders (A1017-18, 1182-83). Schwartz did so (Exhs. K, L, A231, 238; A1026-1154). See pp. 54-55, *infra*.

At the same time, D-Z and Cantor, Fitzgerald actively pursued the prospect of major financing. A number of sources were contacted (A780-810). At one point it appeared that they had achieved success: Cantor, Fitzgerald had introduced Davis to a money lender, Financial Resources Corporation (A786), which—in return for a $5,000 fee—committed itself to lend D-Z $2,700,000 at 6¾% over the prime rate (but in no event less than 15%) (Exh. C, A213-20). D-Z would use the money to finance a tender offer for 350,000 shares of NJB. The commitment letter was executed on June 27 (A794). Almost immediately thereafter it was cancelled: the lawyers had said that because of Cantor, Fitzgerald's role in arranging the financing, the loan would violate the margin regulations (A790-91).* D-Z nonethless continued its efforts to consummate financing arranged by Cantor, Fitzgerald (A810, 1272). And, on July 7, Davis himself "advanced" $75,000 to D-Z to fund further accumulations (A915-16).

In the first days of July, additional heavy purchases of NJB shares were made by Cantor, Fitzgerald on the American Exchange on behalf of D-Z (Exh. A, A207). These purchases came to the attention of the trustees. Discovery was launched in this action which ultimately led to the filing of counterclaims by the trustees and the instant motion for a preliminary injunction (A73-75, 26-57, 69-71).

Both in the proceedings in the court below and in deposition testimony, D-Z and its counsel have made plain that it has in no way abandoned its attempt to take over control of NJB: that, if not enjoined, it will actively continue its

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* Two days before, NJB's counsel had filed counterclaims in this action setting forth that the combined conduct of D-Z and Cantor, Fitzgerald to that date had amounted to margin violations (A39-43).

"accumulation" program of NJB shares (A762); that, if it is successful in obtaining the requisite financing, it will make a formal tender for control (A777).

ARGUMENT

POINT I

The District Court erred in holding that in a takeover fight enforcement of the securities laws is "best left to the SEC or to the stockholders" rather than to the target company itself.

After a chronological review of the background facts and the status of the pleadings, the District Court in Point "1" of its opinion pointed to D-Z's prior unsuccessful attempt to enjoin the NJB shareholders meeting and then wrote:

> Now management moves to restrain D-Z; it seems clear that this motion should also be denied. Management is simply trying to protect its entrenched position* and, while its attackers must obey the securities laws,

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* Elsewhere, the District Court referred to management as being "motivated by a desire to retain its loaves and fishes" (A356). The record upon this motion is devoid of a scintilla of evidence that the trustees are acting in this litigation from any improper motivation. Although D-Z's counsel was afforded extensive depositions of the trustees and documentary discovery prior to the hearing of the preliminary injunction motion, counsel chose neither to seek to introduce, nor to make any reference to, any evidence thus gathered upon the hearing. The evidence that is of record as to the trustees' motivations establishes that the trustees brought the motion below in order to protect the trust and its shareholders, upon learning by means of discovery that: (1) D-Z was proceeding in its takeover bid in flagrant disregard of law; (2) D-Z was planning, if it succeeded in acquiring control of the trust, to destroy its tax-exempt status (see p. 30, *infra*); and (3) D-Z was planning, if it acquired control of the trust, to raid the trust's own assets to repay the borrowings that D-Z had incurred in financing the very stock purchases by which it was attempting to seize control. See p. 30, *infra*.

> *enforcement of those laws is, with rare exceptions, best left to the SEC or to the stockholders of NJB.* (Emphasis added.) (A361)

It is plain that this holding sets the tone for the balance of the District Court's opinion brushing aside the merits of the trustees' claims and is the essential premise of the District Court's rejection of the trustees' standing to make certain of those claims.

It is submitted that this holding by the District Court runs directly counter to the holding and reasoning of this Court in *GAF Corp* v. *Milstein,* 453 F.2d 709, 719-21 (2d Cir. 1971), *cert. denied,* 406 U.S. 910 (1972), that "in the context of struggles for corporate power", it is the target company—precisely because of its "resources" and "self-interest"—that is the *best* party in a position effectively to enforce compliance with the securities laws and protection of the public interest and that, contrary to the view of the District Court, such enforcement cannot be left either "to the SEC or to the stockholders" (A361). The *Milstein* case, although urged below, is nowhere cited or referred to in the District Court's opinion.

In *Milstein,* this Court faced the question of whether, in a takeover context, the target company should be afforded standing to raise violations of the Federal securities laws by the potential acquiring company (the particular violation in question being a claimed false filing of a Schedule 13D). Answering the question in the affirmative, this Court first made reference to its prior precedents holding a target company to have standing to raise the issue of violations of the proxy rules (*Studebaker Corp.* v. *Gittlin,* 360 F.2d 692 (2d Cir. 1966)) and of the tender offer requirements (*Electronic Specialty Co.* v. *International Controls Corp.,* 409 F.2d 937 (2d Cir. 1969)). This Court then concluded that the target company not only had standing to assert the insufficiency of Section 13(d) filings, but was indeed the *best*—and often the *only*—person having the requisite means and motivation to enforce compliance. This Court wrote:

There are compelling reasons in addition to preserving symmetry which mandate that GAF has standing. "In determining who has standing to enforce duties created by statute, a court's quest must be for what will best accomplish the purposes of the legislature." *Electronic Specialty, supra,* at 946. *See also* J. I. Case Co. v. Borak, *supra,* at 433 (". . . it is the duty of the courts to be alert to provide such remedies as are necessary to make effective the congressional purpose"). *GAF, as the issuer, unquestionably is in the best position to enforce section 13(d).* The statute requires a copy of the statement to be sent by registered mail to the issuer (this provision alone might support the issuer's standing), and the issuer, in the course of constantly monitoring transactions in its stock, better than anyone else will know when there has been a failure to file. *Cf.* Comment, 81, Harv. L. Rev. 501, 502 (1967). *Moreover, the issuer has not only the resources, but the self-interest so vital to maintaining an injunctive action. See Electronic Specialty, supra,* at 946. (Emphasis added.)

—453 F.2d at 719-20

In *Milstein,* too, the argument had been made that the shareholders of the target company could themselves act to protect their interests. This Court flatly rejected that contention, holding:

Nor is it realistic to expect shareholders to deter persons from filing inaccurate statements by resort to the anti-fraud provisions. *Stockholders are generally unaware of the necessary background information to judge the truth or falsity of the statements.* Additionally, since the Act does not require the statements to be disseminated to shareholders, they do not have the immediate access of the issuer to the filings. Moreover, there may be instances where no shareholder has purchased or sold shares "in reliance" on the statements. In that event, even if the shareholders had standing, *cf.* Mutual Shares Corp. v. Genesco, Inc., 384 F.2d 540 (2d Cir. 1967) (non-selling shareholder given standing to seek injunctive relief), there would be little incentive to maintain an action. (Emphasis added.)

—453 F.2d at 721

And in sharp contrast to the District Court's view in the case at bar that "enforcement of [the securities] laws" is "best left to the SEC" (A361), this Court in *Milstein*, reasoned:

> It is no answer to the query whether the issuer has standing to seek inju ive relief to respond that the [Securities and Exch ge] Commission can proceed under penal provisions. The issuer is the only party which can promptly and effectively police Schedule 13D filings, for it is fair to assume that it scrutinizes carefully changes in its stock ownership—particularly of the sort which can initiate control. And in Borak, the Court instructed that "[p]rivate enforcement of the proxy rules provides a necessary supplement to Commission action." 377 U.S. at 432, 84 S.Ct. at 1560. Even if the Commission had the requisite manpower to delve into the details of each Schedule 13D filing, it does not have the issuer's day-to-day familiarity with the facts which would enable it to appraise accurately the statements in the Schedule. An already overburdened Commission staff, taxed with reviewing increased filings under the securities acts, should welcome "a necessary supplement" to its action.
>
> —453 F.2d at 721

The *Milstein* rationale—that "in the context of struggles for corporate power", the target company, in seeking to protect its own interest, serves as a private policeman for the public interest as well—is not limited to Section 13(d) cases and has been strongly reiterated since by this and other Courts. See, *e.g.*, *Gulf & Western Industries, Inc.* v. *Great Atlantic & Pacific Tea Co.*, 476 F.2d 687, 698-99 (2d Cir. 1973) (tender offer case; target company denominated "private attorney general"; injunction should be granted "to safeguard the public interest"); *Sonesta International Hotels Corp.* v. *Wellington Associates*, 483 F.2d 247, 250-51 (2d Cir. 1973) (tender offer case; materially misleading statements in Schedule 13D; denial of preliminary injunction *reversed* in furtherance of public interest in full disclosure); *Mosinee Paper Corp.* v. *Rondeau*, [Current] CCH Fed. Sec. L. Rep. ¶ 94,719 at 96,374 (7th Cir., July 16, 1974) (*non*-tender offer case involving fail-

ure to file Schedule 13D—denial of permanent injunction *reversed*—target company, as prime enforcer of public interest in compliance with Section 13(d), need not even show irreparable injury); *Bath Industries, Inc.* v. *Blot*, 427 F.2d 97, 111 (7th Cir. 1970) (*non*-tender offer case—grant of preliminary injunction *affirmed*—where public interest involved, all doubts should be resolved in favor of target company which merely seeks to preserve *status quo*).

It is submitted that the diametrically contrary holding of the District Court in the case at bar, which constitutes the basic premise for that court's rulings against the trustees, cannot be reconciled with these controlling precedents.

POINT II

D-Z's Schedule 13D and the amendments thereto are false and misleading in essential respects.

A. A Schedule 13D serves a vital function in the investment market and cannot be permitted to be false and misleading.

A fundamental ground urged by the trustees below was that the Schedule 13D required to be filed by D-Z upon becoming a 5% stockholder of NJB (as well as the subsequent amendments thereto) were false and misleading in virtually every essential respect (see pp. 26-35, *infra*), and that accordingly under settled principles of law a preliminary injunction was required to issue against continuing stock purchases by D-Z. This principal ground for an injunction was urged by the trustees quite separate and apart from an *additional* and *independent* ground for injunctive relief argued below—and maintained by the trustees in this Court—that D-Z's stock purchase program for obtaining control of NJB viewed in its entirety constituted in contemplation of law a "tender offer" within the meaning of the Williams Act (see Point V, *infra*).

Unfortunately, the court below apparently wholly misconceived the trustees' position. Thus, the court below wrote:

> The basic argument for movants on this point [that the Schedule 13D and amendments filed by D-Z were "false and misleading" in violation of the 1934 Act] *depends entirely on their other argument, already noted, that D-Z had made a "tender offer"*. (Emphasis added.) (A365)

It is surprising that the District Court should have thus misconstrued the trustees' position. At no time did the trustees ever link the "false 13D" and "illegal tender offer" arguments ("entirely" or otherwise)* and when *D-Z* below sought to pretend that the "13D" issue was dependent upon the "tender offer" issue, the trustees unequivocally responded to the District Court:

> The law is clear—*quite apart from any doctrines which come into play in connection with tender offers*—that the Schedule 13D filing required of a 5 percent holder of shares under Section 13(d) of the 1934 Act must make full and truthful disclosures and that an injunction will issue at the instance of the target company for failure of the Schedule 13D to measure up to these standards.[*] (Emphasis added.)
>
> [*] This controlling doctrine of law is, of course, quite separate and apart from the fact that the instant case indeed *does* involve a tender offer, albeit a *de facto* one. [Original footnote, Reply Memorandum, p. 5. (Emphasis in original.)]
>
> —Reply Memorandum, p. 5.

The trustees' "basic argument" below was, thus the precise contrary of that ascribed to it by the District Court's opinion.

More important, however, than the District Court having misconceived the trustees' position: it is submitted that the District Court wholly misconceived the controlling doctrines of law governing the filing of a Schedule 13D as required by Section 13(d) of the Exchange Act by a 5% stockholder. Thus, in the court below, counsel for D-Z argued that whereas an offering circular upon *a tender offer* must meet the general standards of disclosure and

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* In the trustees' original Memorandum of Law below, the "false 13D" issue appears as Point I, the "illegal tender offer" issue as Point IV.

truthfulness required by the securities laws, a Schedule 13D filing—absent a tender offer—was "simply a form with particular items of information called for" and should not be held to any significant standards of disclosure or truthfulness. Plaintiff's Memorandum of Law, p. 23. Rather astoundingly this argument by D-Z was *accepted* by the District Court in its decision. The District Court held (A365-66):

> Counsel for D-Z seem correct in pointing out that the Schedule 13D required of those (such as D-Z) *not* making a tender offer differs from the Schedule 13D required of those making a tender offer (such as *Gulf & Western* in the action already cited).
>
> * * * Such tender offer must not be false or misleading (see Section 14(e) of the 1934 Act). If D-Z were making a tender offer, then its Schedule 13D would be judged in the context of stockholders trying to decide whether to accept the tender offer or not.
>
> D-Z is not making a tender offer. Its Schedule 13D is required simply because it owns more than 5% of the NJB shares.

This crucial holding by the District Court—that whereas stockholders rely upon the truthfulness of a Section 14(d) tender offer in making investment decisions, no comparable reliance exists as to a Section 13(d) Schedule 13D—flies in the face of controlling precedent, including the decision of this Court in *GAF Corp.* v. *Milstein, supra,* the landmark Schedule 13D holding in the Federal Courts, which case is nowhere alluded to in the District Court's opinion.

In *Milstein,* a *non*-tender offer case, this Court was faced with an argument—reiterated, as noted above, in only slightly disguised form by D-Z in the case at bar—that the Williams Act while containing a Section 14(e) expressly imposing a general anti-fraud standard of truthfulness in connection with *tender offer* filings, contained no parallel section imposing such requirements on Schedule 13D filings not made in connection with a tender offer, *i.e.,* those filed pursuant to Section 13(d).

This argument was, however, expressly *rejected* by this Court in *Milstein*. This Court therein held that, notwithstanding the absence of a specific "truthfulness" section applicable to a Section 13(d) filing, such a requirement would be read into the Williams Act, stating:

> The more difficult question is whether GAF has standing under section 13(d) to seek an injunction against allegedly false and misleading filings. The Milsteins in their brief argue that "the short answer" is that false filing does not violate the section that requires the filing—i.e., section 13(d)—but rather the penal provision on false filings, section 32(a), or one of the anti-fraud provisions, for example, section 10(b). This response, deceptively pleasing in its simple, compartmental approach to the Securities Exchange Act, immediately brings to mind the Supreme Court's instruction that the securities acts should not be construed technically and restrictively, but "flexibly to effectuate [their] remedial purposes." S.E.C. v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 195, 84 S.Ct. 275, 11 L.Ed.2d 237 (1963). *With this teaching in mind, we conclude that the obligation to file truthful statements is implicit in the obligation to file with the issuer, and a fortiori, the issuer has standing under section 13(d) to seek relief in the event of a false filing.* (Emphasis added.)
>
> —453 F.2d at 720

In reaching this conclusion that truthfulness was required of a Schedule 13D filed under Section 13(d), this Court rejected the concept that—absent a tender offer—the filing of a Schedule 13D was some mere ministerial formality bereft of pragmatic consequences to the investing public. To the contrary, as this Court in *Milstein* set forth, the legislative purpose behind the Williams Act in general, and Section 13(d) in particular, is

> to alert investors to potential changes in corporate control *so that they could properly evaluate the company in which they had invested or were investing. Disclosure which is false or misleading subverts this purpose.* In some instances, a false filing may be more detrimental *to the informed operation of the securities markets* than no filing at all. (Emphasis added.)
>
> —453 F.2d at 720

That the truthfulness and adequacy of disclosure in a "Section 13(d)" Schedule 13D are relied upon by the public in making investment decisions has—until the decision of the court below—been regularly recognized by the courts. Thus, in *Bath Industries, Inc.* v. *Blot*, 427 F.2d 97, 109 (7th Cir. 1970), the Seventh Circuit, in affirming the district court's grant of a preliminary injunction based upon violation of Section 13(d), stated:

> Our review of the legislative history convinces us that *the overriding purpose of Congress in enacting this legislation was to protect the individual investor* when substantial shareholders or management undertake to acquire shares in a corporation for the purpose of solidifying their own position in a contest over how or by whom the corporation should be managed. In the words of Senator Williams: "[The bill] is designed solely to require full and fair disclosure for the benefit of investors." 113 Cong. Rec. 24664 (1967). *See also* Electronic Specialty Co. v. International Controls Corp., 2 Cir., 409 F.2d 937, 945 (1969). *The protected class of investors includes investors in general as well as the stockholders of the specific corporation involved.* 114 Cong. Rec. 21954. (Emphasis added.)

In light of this purpose, the *Bath Industries* Court held that supposed "corrective" filing of the required Schedule 13D disclosures could prove insufficient to protect the investing public, stating:

> The purpose of the filing and notification provisions is to give investors and stockholders the opportunity to assess the insurgents' plans *before* selling or buying stock in the corporation. It additionally gives them the opportunity to hear from incumbent management on the merit or lack of merit of the insurgents' proposals. (Emphasis in original.)
>
> —427 F.2d at 113

And, in *Nachman Corp.* v. *Halfred, Inc.*, [1973-74] CCH Fed. Sec. L. Rep. ¶ 94,455 (N.D. Ill. 1973), an injunction was ordered for failure of a "Section 13(d)" Schedule 13D adequately to set forth the more-than-5% shareholder's plans with respect to the subject company. The court, citing *Bath Industries*, pointed out (at 95,596):

> The purpose of the filing and notice provisions of § 13(d) of the Williams Act is to give investors the opportunity to assess the acquiring company's plans before they sell or buy stock in the target company. If Halfred does not file this information, there may be no way to remedy the lack of disclosure in the future.

Most recently, in *Mosinee Paper Corp. v. Rondeau*, [Current] CCH Fed. Sec. L. Rep. ¶ 94,719 (7th Cir., July 16, 1974), the Seventh Circuit again rejected the argument that failure to file a true and complete Schedule 13D was a mere "technical violation". The *Mosinee* Court, relying on and quoting from *Bath Industries* and this Court's opinion in *Milstein*, set forth (at 96,374):

> The sweep of section 13(d) goes beyond the circumstances where the purchaser has formulated an intent to control, but also reaches that point when because of the size of the purchaser's holdings (having attained five percent beneficial ownership of a class of stock) and the fact that he acquired such holdings in a short amount of time, the purchaser portends the *potential* to effectuate a change in control. *Under such conditions Congress has deemed it appropriate that investors and management be fully advised of this potential to effect control so that investors may evaluate and adequately assess the corporation's worth in view of the potential, while at the same time allowing management the opportunity to appropriately respond to any potential for a shift in control.*
>
> Congress desired that investors and management be notified at the earliest possible moment of the potential for a shift in corporate control. *To that end, acquisition of five percent of a class of stock was designated as a trigger to bring about full and fair disclosure.* By failing to timely file, Rondeau effectively failed to disclose to investors and management the circumstances surrounding his potential to effect the control of Mosinee Paper while at the same time he continued to purchase securities in a market that had not been adequately apprised of such potential. Under the circumstances, Rondeau's failure to timely file was more than a mere technical violation of the Williams Act. (Emphasis added.)

These judicial precedents do no more than recognize the reality of the marketplace. Thus, where there is a "large, rapid aggregation or accumulation of securities" which operates to trigger Section 13(d),* the Section 13(d) filing requirement then serves precisely the same function of bringing information to the investing public in the *non*-tender offer situation as the Section 14(d) requirement does where a tender offer *is* being made. The key information required by the SEC to be furnished by the more-than-5% holder in his Schedule 13D—details as to his source of funds, including borrowings; specificity of disclosure as to his "purposes" with respect to his acquisitions of stock and "plans" for the company (see Items 3, 4, of Schedule 13D, pp. 27, 31-32, *infra*)—are all carefully designed to permit members of the investing public, "investors in general as well as the stockholders of the specific corporation involved",** to make informed decisions as to whether to buy, sell or hold. Thus—

> How many shares of the subject company does the acquiring company intend to buy?
>
> Over what period of time?
>
> Does it have the financial wherewithal or resources to support major purchases?
>
> How secure is its financial posture: may it be obliged to make a forced sale of blocks of stock in a weakening market thus further depressing the market price?
>
> What is the likelihood of its seeking control: by further market purchases; by a formal tender offer; by launching a proxy fight?
>
> What are its plans for the company if it does acquire control?

—all of this information required to be *truthfully* disclosed in the Schedule 13D is of the utmost importance to the in-

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* *GAF Corp.* v. *Milstein, supra,* at 717. It should be noted that a 5% holding does not in and of itself trigger § 13(d) unless coupled with an acquisititon of 2% of the stock in a twelve-month period.

** *Bath Industries, Inc.* v. *Blot, supra,* at 109.

vesting public in attempting to reach an informed decision:

> Are the plans of the more-than-5% holder with respect to future purchases or a formal tender such that the market price of the stock is likely to rise—or fall?
>
> If the holder takes control, will other shareholders be better served being "in" or "out"?

The investing public is entitled to know that such Schedule 13D must meet the same standards of truthfulness and candor as govern all other securities laws filings.

As this Court recognized in *GAF Corp. v. Milstein, supra*, the congressional intent in enacting Section 13(d) was precisely to require such information to be available for the benefit of the investing public. This Court wrote:

> Specifically we were told, "*the purpose of section 13(d) is to require disclosure of information by persons who have acquired a substantial interest, or increased their interest in the equity securities of a company by a substantial amount, within a relatively short period of time.*" S. Rep. No. 550 at 7; H. R. Rep. No. 1711 at 8, U.S. Code Cong. & Admin. News p. 2818. *Otherwise, investors cannot assess the potential for changes in corporate control and adequately evaluate the company's worth. See generally* Comment, Section 13(d) and Disclosure of Corporate Equity Ownership, 119 U. Pa. L. Rev. 853, 854-55, 858, 865-66 (1971). (Emphasis added.)
>
> —453 F.2d at 717

And as this Court emphasized:

> Disclosure which is false or misleading subverts this purpose. In some instances, a false filing may be more detrimental to the informed operation of the securities markets than no filing at all.
>
> —453 F.2d at 720

In sum, in reaching its holding that D-Z's Schedule 13D was "required simply because it owns more than 5% of the NJB shares" but—unlike a tender offer—would not be the subject of any particular reliance by stockholders, the District Court clearly erred. The District Court's view of the function of a Schedule 13D required by Section

13(d) of the 1934 Act runs directly counter to the reality of the marketplace, the specific intent of Congress in imposing the Section 13(d) requirement and the holding of this Court in *GAF Corp.* v. *Milstein*—wholly ignored in the District Court opinion—as well as the holdings of all other courts that have had occasion to consider the function of a Section 13(d) filing and the standards by which it is to be judged.

B. The Schedule 13D and amendments filed by D-Z fail to meet the standards of truthfulness, candor and adequacy of disclosure required by the Federal securities laws.

It is submitted that the uncontradicted record proofs offered by the trustees—the admissions upon deposition of D-Z's own witnesses and the documentary evidence from D-Z's own files—establish that D-Z's Schedule 13D and the amendments thereto are false, misleading and incomplete in essential respects. The District Court failed to make any findings of fact with respect to this evidence: rather, the District Court in its opinion (A366) summarily dismissed all such proofs without elaboration or explanation in a single, conclusory sentence: "It is not shown that the Schedule 13D or any amendment is false or misleading."*

As previously noted, inasmuch as no live testimony was heard by the District Court, this Court need give no special deference to the District Court's findings, since it is "in as

* Although the District Court may incorporate findings of fact into its opinion, it is well settled that mere conclusory statements of ultimate finding in broad and general terms, without underlying analysis or justification, does not satisfy the requirement of Rule 52(a) of the Federal Rules of Civil Procedure that "in refusing an interlocutory injunction the court must set forth the findings of fact * * * upon which it predicates grounds of its action." *Bateman* v. *Ford Motor Co.,* 310 F.2d 805, 807 (3d Cir. 1962). See also *Russo* v. *Central School Dist. No. 1, etc.,* 469 F.2d 623, 628-29 (2d Cir. 1972); *Bose Corp.* v. *Linear Design Labs, Inc.,* 467 F.2d 304, 311 (2d Cir. 1972).

good a position as the trial court to examine", read and interpret the depositions, exhibits and affidavits. See p. 7, *supra.* It is submitted that review of the incontrovertible record evidence must lead this Court to the conclusion that the District Court erred in its view of the facts. Without attempting to reiterate in detail each of the instances of falsity demonstrated by the record, it will be shown herein that the D-Z Schedule 13D is false and misleading in crucial respects: (1) as to its failure to disclose D-Z's "purposes and plans" with respect to NJB; and (2) as to D-Z's "source and amount of funds" for its NJB purchases.

1. *Falsity and failure of disclosure with respect to D-Z's "purposes and plans".*

Pursuant to Rule 13d-1 adopted by the SEC, a Schedule 13D is required to set forth the 5% holder's purpose or purposes in the transaction as well as any plans for significant changes in the business or corporate structure of the subject company if control is achieved. Specifically, Item 4 of Schedule 13D ("Purpose of Transaction") requires the holder to:

> State the purpose or purposes of the purchase *or proposed purchase of* securities of the issuer. *If the purpose or one of the purposes* of the purchase or proposed purchase *is to acquire control of the business of the issuer, describe any plans or proposals which the purchasers may have to liquidate the issuer, to sell its assets or to merge it with any other persons, or to make any other major change in its business or corporate structure,* * * *. (Emphasis added.)

A failure to set forth any such plans renders the Schedule 13D "false and misleading." See, *e.g., General Host Corp.* v. *Triumph American, Inc.,* 359 F. Supp. 749, 753-56 (S.D.N.Y. 1973); *Nachman Corp.* v. *Halfred, Inc.* [1973-1974] CCH Fed. Sec. L. Rep. ¶ 94,455 at 95,593-94 (N.D. Ill. 1973). And an "intention" held at the time of filing the Schedule 13D constitutes a "plan or proposal" even though it has not yet reached the stage of possibly coming to fruition. See *In the Matter of the Reports of the Sus-*

quehanna Corp., Sec. Exch. Act Rel. No. 8933, [1969-70] CCH Fed. Sec. L. Rep. ¶ 77,842 at 83,987-88 (1970); *Matter of the Susquehanna Corp.*, SEC Admin. Proc. No. 3-1868, [1968-70] CCH Fed. Sec. L. Rep. ¶ 77,741 at 83,696-700 (1970). See also *Sonesta International Hotels Corp.* v. *Wellington Associates*, 483 F.2d 247, 251 (2d Cir. 1973) (to be material a statement "need not necessarily relate to a past or existing condition or event. It may refer to a prospective event, even though the event may not occur, provided there appears to be a reasonable likelihood of its future occurrence"). *But cf. Missouri Portland Cement Co.* v. *Cargill, Inc*, [1973-74] CCH Fed. Sec. L. Rep. ¶ 94,595 at 96,095-25 (2d Cir., June 10, 1974) (mere intention to expand acquired company is not a "change"; no evidence in record that any such "plan" was developed or adopted).

It is clear from the record that D-Z's Schedule 13D failed to make adequate disclosure of D-Z's intentions with respect to its proposed purchases of shares of NJB and for major changes in NJB's business and corporate structure once control was achieved.

Thus, *with respect to "purchases" and "proposed purchases"*, D-Z's Schedule 13D reported the purchase of 71,200 shares of NJB and then set forth that "[d]epending upon future circumstances not now known, D-Z may take such action from time to time as it may deem appropriate, in the light of future developments, in order to obtain control of NJB and for the best interests of NJB," which actions "may include: (1) Acquisition of additional NJB Shares * * *" (Exh. C, A114). This "disclosure" was false and misleading. In fact, it is now conceded that—in sharp contrast to the pious generalities of the D-Z Schedule 13D—at the time of the filing of that Schedule 13D, D-Z had formulated a specific plan to acquire a very precise number of the shares of NJB, to wit, 300,000 of such shares (representing approximately 25% of the total outstanding stock) (A393-95, 776) and that D-Z at the very time of filing of the Schedule 13D was actively engaged in implementing this precise plan (A480-96, 505-08, 646-52, 827-46). Not a breath of disclosure of this plan appears in D-Z's Sched-

ule 13D. It is difficult to conceive of a fact more material to a member of the investing public in determining whether to buy, sell or hold shares of NJB than disclosure of such a specific plan of acquisition of shares by an acquiring company.*

With respect to plans to make any "major change" in NJB's "corporate structure", D-Z's Schedule 13D speaks wholly in conditional generalities of possible actions D-Z "may" find "desirable to recommend" if it should obtain control, "subject to a study of all of NJB's assets and all other relevant circumstances then obtaining" (Exh. C, A113-15). D-Z's Schedule 13D, moreover, expressly denied, "[e]xcept as mentioned above," that D-Z had any "present intention" with respect to NJB "nor has it in any event formulated any specific plan or proposal * * * to make any major change in its business or structure" (Exh. C, A115). Once again, however, the incontrovertible record evidence—in this case the documentary proof of explicit written statements of plans by D-Z's president and chief executive officer, Davis (Exh. D, A221-24; Exh. 25, A1747)**—categorically establishes the falsity and lack of candid disclosure in the Schedule 13D. Thus, Davis in his written statement sets forth quite unconditional and explicit "present intentions" and "plans" with respect to NJB's corporate structure, including that

> (1) "[a]t some point in time, we would cancel the advisory contract [*i.e.*, the agreement between the trust and its investment advisor]" and "[w]e would install our people as the trustees of the trust and, in addition form our own advisory Company" (Exh. D, A223);

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* Facts are "material" if "a reasonable investor might have considered them to be important" in making his investment decision. See, *e.g.*, *Sonesta International Hotels Corp.* v. *Wellington Associates*, *supra*, at 251.

** These express statements of plans were written by Davis in the form of letters to be utilized, and which were utilized, in an effort to raise funds to finance D-Z's takeover of NJB. One such letter was written by Davis to the Morgan Guaranty Trust Company (Exh. 25, A1747); another was directed to Davis' own business associate, Saul Becker (Exh. D, A221-24).

(2) as an interim measure, the trust status would be maintained so that "servicing of the debt incurred in the acquisition of the trust can be accomplished via the trust's earnings which are passed through to the shareholders" (Exh. D, A223);

(3) but then, "the next step would be to gain voting control of 66⅔% of the outstanding shares *and vote to eliminate the trust type of ownership*" (Exh. D, A224) (emphasis added);

(4) then, "I would use the corporation as a vehicle to tender for other trusts which meet the percentage criteria of market value to book value and have acceptable loan portfolios" (Exh. D, A224);

(5) then, "It is also my intention to merge our operating company into the corporation on a stock-for-stock basis" (Exh. D, A224); and

(6) finally, *the assets of the trust itself would be used to repay the indebtedness that the promoters had incurred to acquire control*—as Davis blatantly sets forth: "The corporation has sufficient value and assets to retire the original indebtedness" (Exh. D, A224). See also Exh. A, A108-09.

These very precise "present intentions" and "plans" had been formulated by Davis prior to the filing of the D-Z Schedule 13D and the evidence shows they were likewise held at the time of such filing (A762-65). Once again, it is difficult to conceive of facts more material to members of the investing public in determining whether to stay "in" NJB or get "out" than these quite precise plans of Davis to destroy the REIT's tax-exempt status (the very *raison d'etre* for most shareholders' investment in the first instance) and to raid the trust's own assets to repay the borrowings incurred by D-Z for the very purpose of purchasing its control position in NJB. See, *e.g.*, *Sonesta International Hotels Corp.* v. *Wellington Associates*, *supra*, at 251 (facts are "material" if "a reasonable investor might have considered them to be important" in making his investment decision); *General Host Corp.* v. *Triumph American, Inc.*, *supra*, at 753-56 (failure of Schedule 13D to disclose that acquiror intended to convert subject company's assets to cash in order to repay cost of acquisition

was material); *Nachman Corp.* v. *Halfred, Inc., supra,* at 95,593-94 (acquiror's proposals for dissolution and merger are material and must be disclosed in a Schedule 13D).* And, once again, it is clear that such "present intentions" held by Davis were required to be candidly disclosed in the D-Z Schedule 13D. See *e.g., In the Matter of the Reports of the Susquehanna Corp., supra,* at 83,987-88; *Matter of the Susquehanna Corp., supra,* at 83,696-700; see also *Sonesta International Hotels Corp.* v. *Wellington Associates, supra,* at 251 (disclosure of potential future events).

With respect to plans to make any "major change" in NJB's "business", once again the record shows an abysmal failure of candid disclosure in the D-Z Schedule 13D. For it is conceded in the deposition testimony that Davis had in fact formulated very precise and detailed plans for the disposition of major segments of NJB's real estate portfolio should D-Z acquire control (A556-57). The properties in question had been physically inspected and analyzed; determinations had been made as to just which would be retained, which would be disposed (A557-58).** These "plans" and "present intentions", too, were held at the time of the filing of D-Z's Schedule 13D and the amendments thereto (A557-58). These "plans" and "present intentions", too, were not only not disclosed in the 13D but were expressly denied to exist (Exh. C, A115).

2. *Falsity and failure of disclosure with respect to D-Z's "source and amount of funds".*

Item 3 of Schedule 13D requires the filing party to:

> State the *source and amount of funds* or other consideration *used or to be used in making the purchases,*

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* The facts of the present case thus bear no resemblance to those in *Missouri Portland Cement Co.* v. *Cargill, Inc., supra,* at 96,095-25, where this Court found that a mere "intention to expand the acquired company" did not constitute a "change" and that there was no evidence that any "plan" had ever in fact been developed.

** Cantor, Fitzgerald's Orbe admitted that Davis and his associates "then made detailed physical inspections of those problem properties and formulated specific ideas with respect to each one" (A577).

and if any part of the *purchase price or proposed purchase price is represented or is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading the securities, a description of the transaction* and the names of the parties thereto. (Emphasis added.)

On the uncontradicted record evidence, D-Z's Schedule 13D is massively false, misleading and inadequate with respect to the funds being used and planned to be used by D-Z in financing its takeover bid. Nowhere does D-Z's Schedule 13D remotely disclose that D-Z is a "shell" corporation formed just days before with a *total* capitalization of only $10,000 (A435-36).* It is this $10,000 "source of funds" that was to provide the sole equity base for the inverted pyramid of borrowings by which D-Z is planning to gain control of NJB, a listed company, with 1,276,053 outstanding shares. Notwithstanding the express requirements of Item 3, no disclosure of the "amount" of this $10,000 "source of funds" or "description of the transaction" in which they were obtained is made in D-Z's Schedule 13D. And nowhere does D-Z's Schedule 13D disclose the critical fact that D-Z is planning to finance *all* of its proposed purchases of the shares of NJB *100%* with borrowed money.**

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* Zimmerman and a corporation controlled by Davis (Security Management Co., Inc.) each purchased 50 shares of D-Z stock at $100 per share (A435-36).

** Moreover, notwithstanding that D-Z was an unknown company and that there was a "total unavailability of any financial information regarding [D-Z] to the holders of [NJB shares]," D-Z's Schedule 13D is devoid of any financial statement as was expressly held to be required in such circumstances in *Corenco Corp* v. *Schiavone & Sons, Inc.*, [1973] CCH Fed. Sec. L. Rep. ¶ 94,099 at 94,432-94,433 (S.D.N.Y.), *aff'd in part and remanded in part on other grounds*, 488 F.2d 207 (2d Cir. 1973); see also *Corenco Corp.* v. *Schiavone & Sons, Inc.*, [1973] CCH Fed. Sec. L. Rep. ¶ 94,220 (S.D.N.Y. 1973) (upon remand). The holding in *Corenco* applies *a fortiori* to the present case where D-Z was a newly-minted corporate entity with a sole capitalization of $10,000 and was therefore planning ultimately to raid the assets of the trust itself to re-pay 100% borrowings incurred in the takeover

(footnote continued on following page)

Rather, D-Z's "Item 3" simply states that, for the shares already purchased "$254,783 * * * were obtained by D-Z in a [supposed] private placement of its 6% promissory notes [totalling $350,000, the identity of the notes purchasers being specified]" and that the balance "was obtained by margin borrowings of $3 per share from Cantor, Fitzgerald * * *" (Exh. C, A113). This "disclosure" is not only affirmatively false in that the notes transaction purported to be described was in fact not "a private placement" but rather a "public offering" (see pp. 46-52, *infra*),* but also wholly *fails* to reveal:

> that the $350,000 in promissory notes already sold were but a part of a much larger issue of such notes (Exh. G, A133);
>
> that D-Z had authorized an issue of $1,250,000 of such promissory notes (Exh. G, A133);
>
> that D-Z was actively engaged in attempting to sell that entire $1,250,000 issue—through the device of a so-called "Private Placement Memorandum" prepared and being circulated for that purpose, see pp. 48-52, *infra;*
>
> that D-Z had formulated an express plan to join the $1,250,000 proceeds of such note offer with margin loans to provide a $2,200,000 wherewithal of borrowings to finance the purchase of 300,000 NJB shares (A391-98).**

(*footnote continued from preceding page*)

attempt. The members of the investing public—in making their day-by-day decisions whether to buy, sell or hold NJB shares in the face of D-Z's plans—were indisputably entitled to have D-Z's Schedule 13D include a simple financial statement.

* In Point III of this brief, appellants will set forth that D-Z's promissory note issue was illegal and voidable under the 1933 Act, the 1940 Act and the margin regulations, and that such illegality and the invalidity of the borrowing was required to be disclosed in Item 3 of D-Z's Schedule 13D as part of the "description of the transaction" required where funds have been borrowed by the filing party.

** Likewise not disclosed is that, according to the "Private Placement Memorandum", all of the shares issued by D-Z to Davis and Zimmerman—which shares in turn controlled D-Z's sole asset, the NJB shares purchased by D-Z—were required to be placed in escrow as collateral to secure the 6% promissory notes (Exh. G, A139). The NJB shares were thus, in essence, to stand twice as collateral: first for the formal margin loans; then for the noteholders.

No disclosure of such financing program of funds "to be used in making the purchases" appears anywhere in D-Z's Schedule 13D.

And, finally, nowhere does D-Z's Schedule 13D even hint at the fact that the climax of D-Z's entire plan of financing its purchases has always been to use the very assets of NJB itself as the source of repayment for the entire indebtedness that D-Z would incur in the takeover, see p. 30, *supra*: that it was NJB's own assets that were to be the ultimate "source of funds" for D-Z's purchases. *Cf. General Host Corp.* v. *Triumph American, Inc., supra.**

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* Nor is the falsity and lack of disclosure of D-Z's original Schedule 13D cured in any respect by any of the six amendments thereafter filed. To the contrary, the amendments themselves are affirmatively false and misleading in failing to disclose ongoing events. By way of example only:

> that in late May, D-Z actually retained the proxy solicitation firm of Georgeson & Co., paying Georgeson a $5,000 retainer and contracting to pay $25,000 for proxy solicitation services (Exh. 22, A1745; A963-66);
>
> that when sales of D-Z's 6% promissory note issue faltered, D-Z had determined to seek alternative sources of financing and was actively negotiating for massive borrowings at staggering rates of interest—*e.g.*, 6¾% *over* the prime rate (but in no event lower than 15%) (Exh. C, A213);
>
> that in late June, D-Z had formulated a specific plan to make a formal tender offer for 350,000 shares of NJB (Exh. C, A213-20; A786-89)—a plan that was then supposedly "abandoned" for want of financing but subject to resurrection should the necessary funds become available (A777, 789-99);
>
> that on June 27, 1974, D-Z had entered into a formal commitment letter (paying a $5,000 commitment fee) for a $2,700,000 loan to finance such tender offer (Exh. C, A213-20; A786-89)—which commitment was then hurriedly cancelled in the face of this very litigation as concededly constituting a blatant violation of the margin regulations (A789-99);
>
> that D-Z was actively soliciting stock purchases of NJB shares by private communication with shareholders (A690-95, 1026-1154, 1175-76) and had placed orders for purchases of unlimited quantities of NJB shares on the open market (A570, 573-74, 649).

Once again, *none* of these ongoing facts—of the most vital nature to the investing public in assessing D-Z's intentions and the likely impact of those intentions upon the market price of NJB shares—is disclosed in any of the Schedule 13D amendments.

It is submitted that a filing such as that made by D-Z in the case at bar makes a mockery of the entire purpose and function of Section 13(d). On the incontrovertible record evidence, D-Z's Schedule 13D fails to make adequate disclosure and is false and misleading. The unexplained, single-sentence conclusion by the District Court to the contrary is clearly erroneous and must be rejected.

POINT III

The funds being utilized by D-Z in its purchases of NJB stock have been raised in violation of the margin regulations and the securities laws. The target company has standing to obtain injunctive relief.

A major issue upon the present appeal is whether a target company of a takeover bid has the standing to raise the issue that the acquiring company has violated the margin regulations and the securities laws in raising the funds that it is using to finance the takeover. The District Court held it did not (A361, 362). The District Court—in single conclusory sentences without supporting findings or explanation—also held that "no showing has been made of any violation" (A361, 362).

It is submitted that the District Court erred on both grounds: *First,* that the target company has standing to seek injunctive relief against purchases of its stock being illegally financed in violation of the margin regulations and securities laws. *Second,* that the record establishes that D-Z's financing of its stock purchases has indeed been accomplished in clear violation of the margin regulations, the 1933 Act and the 1940 Act, and that D-Z failed in its Schedule 13D to disclose the illegality and voidable nature of its "source of funds".

A. The target company has standing to obtain injunctive relief against purchases of its stock being illegally financed in violation of the margin regulations and the securities laws.

This appeal presents this Court with the opportunity to answer a question of major import to the legal and corporate communities: is a target company powerless to defend

itself from a takeover bid in which the acquiring company is using borrowed funds to finance purchases of the target's stock, which borrowed funds have been raised in violation of the margin regulations and the securities laws.

It is submitted that sound policy and proper construction of the securities laws alike require that the target company not be deprived of standing.

First, parity of reasoning with cases which have afforded the target company standing to raise issues of the illegality of a proxy solicitation by the acquiring company,* illegality of a tender offer by the acquiring company,** illegality of a Schedule 13D by the acquiring company,***likewise inevitably compels the conclusion that the target company should have standing to raise the issue of the illegal funding of its stock purchases by the acquiring company. For, in this instance, as in the others, it is the target company—and the target company alone—that has both the "resources" and the "self-interest" "so vital to maintaining an injunctive action" and is the ideal private policeman to monitor those transactions by which large amounts of its stock are acquired in rapid fashion. See Point I, *supra*; see *GAF Corp.* v. *Milstein*, *supra*; see also *Gulf & Western Industries, Inc.* v. *Great Atlantic & Pacific Tea Co.*, 476 F.2d 687, 698-699 (2d Cir. 1973); *Mosinee Paper Corp.* v. *Rondeau*, [Current] CCH Fed. Sec. L. Rep. ¶ 94,719 at 96,374 (7th Cir. July 16, 1974).****

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* *Studebaker Corp.* v. *Gittlin*, 360 F.2d 692 (2d Cir. 1966).

** *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937 (2d Cir. 1969); *Gulf & Western Industries, Inc.* v. *Great Atlantic & Pacific Tea Co.*, 476 F.2d 687 (2d Cir. 1973); *Sonesta International Hotels Corp.* v. *Wellington Associates*, 483 F.2d 247 (2d Cir. 1973).

*** *GAF Corp.* v. *Milstein*, 453 F.2d 709 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972).

**** It is emphasized that no contention is being made on this appeal that the target company would have standing to seek *damages*, say for violation of the 1933 Act or to seek *rescission* of the illegal note purchase transactions as between D-Z and its noteholders. Rather, it is appellants' position that the target company has standing to seek *injunctive* relief limited to restraining the purchases of *its own stock* with the use of the illegally raised funds. The distinction between standing to obtain appropriate injunctive relief as contrasted with standing to obtain damages has frequently been recognized by this Court. See, *e.g.*, *GAF Corp.* v. *Milstein*, *supra*, at 720 n.22; *Mutual Shares Corp.* v. *Genesco, Inc.*, 384 F.2d 540, 546-47 (2d Cir. 1967).

Indeed, the factors which have dictated "standing" in the "proxy", "tender" and "13D" areas apply with particular cogency in the "illegal source of funds" area. For, once again, there is essentially no one *other* than the target company available to do the job. The selfsame factors which led this Court in *GAF Corp.* v. *Milstein* to reject the SEC and the stockholders of the target company as sufficient guardians of the public interest apply equally in the case at bar. And the target company has a unique interest in protecting against large blocks of its stock being purchased with illegally raised funds. *Cf. Diamond* v. *Oreamuno,* 24 N.Y.2d 494, 499 (1969) (a corporation has "great interest in maintaining a reputation of integrity, an image of probity, for its management and in insuring the continued public acceptance and marketability of its stock").

Moreover, where its stock is purchased without adequate equity in violation of the margin regulations, there is the omnipresent danger that in the event of a downturn in price, large blocks of stock would be forced to be involuntarily dumped on the market, thus inexorably accelerating the rate of market decline and occasioning a major disruption in the orderly market of trading in its shares. Thus as noted in Senate Report No. 1280, 84th Cong., 1st Sess. 41 (1955):

> The excessive use of credit in the securities market * * * may have serious unstabilizing effects, as was the case in the late twenties. * * * The excessive use of credit for buying and carrying securities accentuates market downswings. Those who hold stocks which are financed by credit may be forced by the lender to sell in order to protect the loan. This can lead to additional selling and as stock prices go even lower, others with stocks financed by credit may be forced to unload. At its worst, this type of chain reaction contains the danger of making a market break more serious and disorderly.

See also Federal Reserve Board Chairman Martin's testimony in Stock Market Study, Hearings before Senate Com. on Banking & Currency, 84th Cong., 1st Sess. 549-51 (1955); 15 Stock Exchange Practices, Hearings before Senate Com. on Banking & Currency, 73d Cong., 1st Sess. 6494 (1934); 2 Loss, *Securities Regulation* 1242-43 (2d

ed. 1961). The memory of the 1929 crash was vivid in the minds of the draftsmen of the 1934 Act. See H.R. Rep. No. 1938, 73d Cong., 2d Sess. 8 (1934), as quoted in *Cooper* v. *Union Bank*, [1973] CCH Fed. Sec. L. Rep. ¶ 93,915 at 93,656-57 (C.D. Cal. 1973). Where its stock is purchased with the use of funds that are raised in transactions that are illegal under the Securities and Investment Company Acts and are consequently voidable at the instance of the persons supplying the funds, an identical danger exists.* In fact, it is difficult to conceive of an issue of more vital concern and legitimate interest to the target company than that the very source of funds being used in the acquiring company's takeover bid have been raised in violation of the securities laws.

Recognizing these considerations, the District Court in this Circuit has accorded standing to a target company to raise the issue of violation of the margin regulations. Thus, in *Metro-Goldwyn-Mayer, Inc.* v. *Transamerica Corp.*, 303 F. Supp. 1354, 1357 (S.D.N.Y. 1969), Judge Tenney of the District Court explicitly held that the target company in a tender offer context had standing to raise the contention that the funds borrowed by the acquiror to finance its purchases of the target's shares were obtained in violation of the margin rules. And in *General Host Corp.* v. *Triumph American, Inc.*, 359 F. Supp. 749 (S.D.N.Y. 1973), Judge Pierce implicitly reached the same conclusion.**

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* By way of example, it does not require too much prescience to anticipate that in the case at bar, D-Z's noteholders—who advanced their funds to D-Z for purchase of NJB shares at a time that NJB was trading at $7 per share—may, now that their investment is trading at only $4 per share (9/12/74), be only too happy to find an "out" from an unfortunate investment and—once persuaded that D-Z's takeover bid will fail—will readily seize upon their right of rescission under the 1933 and 1940 Acts.

** Judge Pierce held (at 759) that:

> [T]here is an alleged violation of the margin requirements of the securities law which presents serious questions going to the merits and requires a complete record upon a trial in order that findings of fact essential to a determination of the issue may be made.

—thus necessarily recognizing the target company's standing to raise the issue. The question of standing had been fully briefed before him. Neither *M-G-M* nor *General Host* is referred to in the decision of the court below.

Moreover, quite apart from the trustees' "direct" standing to raise the illegality of D-Z's financing scheme, it is submitted that the trustees must indisputably be deemed to have standing under Section 13(d) to raise the consequent falsity of D-Z's Schedule 13D with respect to its "source of funds". *GAF Corp.* v. *Milstein, supra,* at 720-21. As has previously been detailed, D-Z in Item 3 of its Schedule 13D was obligated to set forth the source and amount of funds "used or to be used" in making its purchases of NJB shares and, to the extent that borrowings were involved, "a *description* of the transaction". D-Z in fact *recognized* this obligation and in its Schedule 13D purported to set forth a description of the transaction, to wit, that the funds used "were obtained by D-Z in a private placement of its 6% promissory notes" (Exh. C, A113). However, as will be hereinafter detailed in this brief, see pp. 46-52, *infra,* this "description" was grievously false: the funds were *not* obtained "in a private placement"; the funds were in fact obtained in an unregistered and illegal public offering of the D-Z note issue.

The District Court, in ruling that the trustees did not have standing to raise any issue of violation by D-Z of the 1933 Act (as well as the 1940 Act and the margin regulations), thus of necessity ruled—in the face of the square contrary holding of this Court in *GAF Corp.* v. *Milstein*—that the trustees did not have standing to raise the issue of the falsity of the "source of funds" Item of D-Z's Schedule 13D. The logical consequence of the District Court's holding on standing would thus be to transform Item 3 of Schedule 13D to read:

> if any part of the purchase price or proposed purchase price is represented or is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading the securities, a description of the transaction and the names of the parties thereto *except that if the transaction by which the funds are borrowed is illegal, voidable or void, the description of the transaction need not so disclose.*

The patent absurdity of any such reading of the Schedule 13D requirement is self-evident. It is difficult to conceive of any facts involved in a "description of the transaction"

of the borrowing which supplies the 5% holder's "source of funds" that is *more* crucial than the fact that the entire borrowing was illegal and is voidable at any time at the instance of the lender. *Cf. Gulf & Western Industries, Inc.* v. *Great Atlantic & Pacific Tea Co., supra,* at 697 ("possibility" of antitrust liability resulting from acquisition of target company's stock had to be disclosed in offering circular); *Sonesta International Hotels Corp.* v. *Wellington Associates, supra,* at 254 ("possibility" of loss of listing on Exchange required to be disclosed).

It is submitted that none of the cases relied upon by the District Court in support of its "no standing" conclusion compel any such result. All such cases—with one exception*—were decided before this Court's decision in *GAF Corp.* v. *Milstein,* which firmly established the principle that the target company has standing to assert every manner of falsity in a Schedule 13D filing. All such cases—with the same exception—are *pre*-Williams Act cases. Thus, although this Court's decision in *SEC* v. *General Time Corp.,* 407 F.2d 65 (2d Cir. 1968), *cert. denied,* 393 U.S. 1026 (1969)—that a target company did not have standing to raise an Investment Company Act violation—was decided shortly after the enactment of the Williams Act, the events at issue had occurred prior thereto and this Court's decision does not take into consideration any Williams Act impact. Moreover, it is instructive to note that *SEC* v. *General Time Corp.* is conspicuous by its absence from this Court's rollcall in *GAF Corp.* v *Milstein* of its controlling precedents as to a target company's standing to raise violations of the securities laws on the part of the acquiring company. It is submitted that whatever continuing validity *SEC* v. *General Time Corp.* may have on its precise non-Williams Act facts,** it is not a precedential holding on

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* To the extent that the court in *Nachman Corporation* v. *Halfred, Inc.,* [1973-74] CCH Fed. Sec. L. Rep. ¶ 94,455 (N.D. Ill. 1973) held to the contrary, it is submitted that such decision is erroneous and is squarely at odds with the rationale of this Court in *Milstein* and the District Court's decisions in *Metro-Goldwyn-Mayer* and *General Host.*

** In *Independent Investor Protective League* v. *SEC,* 495 F.2d 311, 312 (2d Cir. 1974)—a non-Williams Act and non-takeover

(footnote continued on following page)

the issue of a target's standing under Section 13(d) or Section 14(d) to raise the issue of falsity of the acquiring company's filings. It is on these Williams Act issues that this Court has since repeatedly and forcefully emphasized the salutary role of the target company as private policeman and "private attorney general" to monitor the adequacy and truthfulness of such filings in the public interest. *GAF Corp.* v. *Milstein, supra,* at 719-21; *Gulf & Western Industries, Inc.* v. *Great Atlantic & Pacific Tea Co., supra,* at 698-99; *Sonesta International Hotels Corp.* v. *Wellington Associates, supra,* at 250-51.

B. D-Z's funds have been raised in violation of the margin regulations, the 1933 Act and the 1940 Act.

1. D-Z's funds were raised in violation of the margin regulations.

It is clear that D-Z's borrowings of *100%* of its purchase price for the shares of NJB, a listed security, constitute a violation of the margin regulations and that the District Court's one-sentence conclusion of the legality of these borrowings—which D-Z below had not even attempted in its brief to sustain against the trustees' showing of illegality*—is in error.

As noted, the sole capital of D-Z was $10,000 (A435-36). The sole purpose of D-Z's existence was to purchase shares of NJB (A377, 1279-81). Upon this $10,000 base, D-Z set out in combination with its investment banker, the broker-dealer Cantor, Fitzgerald, to borrow—through a combination of "traditional" margin loans and note borrowings—100% of the funds required to purchase such NJB shares (A634-35, 653-57, 660-64). Such borrowings violated the margin regulations promulgated by the Federal Reserve Board pursuant to Section 7 of the Securities Exchange Act of 1934.

(footnote continued from preceding page)

case—this Court expressly left open the question of whether "*only* investors [in the investment company itself] have standing under the Act." (Emphasis in original.)

* See Plaintiff's Memorandum in the District Court, pp. 52-55.

By virtue of Section 7(c) of the 1934 Act and § 220.7 of Regulation T, a broker-dealer such as Cantor, Fitzgerald is prohibited "directly or indirectly" from "arranging" for any other person to extend credit with respect to a margin security in excess of that which the broker-dealer would itself be permitted to loan—*i.e.*, 50% of the purchase price. Participation by the broker-dealer in a plan for the extension of credit by another person constitutes an "arranging" of credit. See Ruling, Board of Governors of the Federal Reserve System, 12 C.F.R. § 220.109.

The record evidence in the case at bar indisputably establishes that Cantor, Fitzgerald was actively participating with D-Z in D-Z's plan to borrow 100% of the funds to be used to purchase shares of NJB. Indeed, the evidence shows that the role of Cantor, Fitzgerald has far transcended that of a mere broker-dealer and has been so pervasive as to constitute Cantor, Fitzgerald a virtual alter ego for D-Z in the takeover attempt. Thus:

> As early as January, 1974, Cantor, Fitzgerald was solicited by Davis for its cooperation and guidance in formulating a takeover plan of some other company (A518-25);
>
> Shortly thereafter, Cantor, Fitzgerald agreed to act as investment banker for Davis' endeavor (A550-51, 660, 689-90; Exh. 28, A1751);
>
> Cantor, Fitzgerald worked closely with Davis in screening a large group of REITs as potential takeover candidates (A542-48, 551-53, 753-54) and it was actually Cantor, Fitzgerald itself that ultimately brought the focus to bear upon NJB (A553, 601);
>
> Cantor, Fitzgerald then proceeded to contact the NJB management to attempt to enlist its cooperation in a "friendly" takeover (Exh. B, A110; A606-08);
>
> Cantor, Fitzgerald has contractually obligated itself to use its best efforts to provide "traditional" margin loans to D-Z to finance a portion of the purchase price of the NJB shares (Exh. B, A291; A659-60);
>
> Cantor, Fitzgerald itself proceeded to provide such "traditional" margin loans to D-Z (A620), and when its own lending limit was exhausted, proceeded to ar-

range additional "traditional" margin loans from other broker-dealers (A924-28, 937)—Ladenburg, Thalmann & Co. (A620-27, 937-41) and Schweikart & Co. (A1270);

Cantor, Fitzgerald both itself provided and arranged for such "traditional" margin loans to be provided by other broker-dealers, with full knowledge that D-Z was *in addition* borrowing the entire balance of the necessary purchase price from other sources (A634-35, 653-57), and was in fact engaged in *100%* borrowings to finance its purchases (A660-64);

Cantor, Fitzgerald's efforts to arrange financing for D-Z's purchases did not stop with both providing and arranging for "traditional" margin loans by broker-dealers. Rather: (i) Cantor, Fitzgerald sought as well to arrange borrowings for D-Z from a number of banks (A696-98, 928-36, 943-47) and ultimately did arrange a borrowing for D-Z, secured by NJB shares, from one such bank (A920-24, 943-54); (ii) Cantor, Fitzgerald in March sought out CNA Financial Corporation to provide the financing for a joint venture (A598-605) that was then agreed upon to make a formal tender offer for approximately 640,000 shares of NJB stock (Exh. A, A108; A608-13, 767-71)—the joint venture was then terminated when CNA developed takeover problems of its own (A628-29, 642-43, 774-75); (iii) when D-Z's promissory note sales faltered, Cantor, Fitzgerald actively sought to solicit major borrowings for D-Z from a number of "sources" (A768-99, 809-22) and was actually successful in June in obtaining a financial commitment from one such "source", Financial Resources Corp., to loan D-Z $2,700,000 to finance a formal tender offer for 350,000 NJB shares (Exh. C, A213-20; A786-89)—this particular financing was hurriedly terminated in the face of this litigation as being concededly illegal under the margin regulations*

* It is noteworthy that Orbe, the Cantor, Fitzgerald vice president who personally participated in procuring the Financial Resources Corp. financial commitment for D-Z, sought—when questioned upon deposition only 20 days later—to conceal the whole transaction by falsely denying any Cantor, Fitzgerald role in any such "efforts, direct or indirect * * * to supply financing, provide financing, ascertain the possibility of a source of financing to Security, Mr. Davis or D-Z" (A696, 698, 178-180). The facts of the Financial Resources transaction—and, ultimately, of Cantor, Fitzgerald's role therein—were not uncovered until a document revealing the transaction was subsequently produced by D-Z upon document discovery (A176-80).

(A789-99); (iv) D-Z nonetheless is continuing its efforts to consummate financing arranged by Cantor, Fitzgerald (A810, 1272);

Cantor, Fitzgerald has generally acted as an alter ego for D-Z in its efforts to take control of NJB: in a telephone solicitation campaign seeking to purchase blocks of NJB stock from existing shareholders; in a telephone solicitation campaign seeking proxy consents to call a special meeting of shareholders (see pp. 54-56, *infra*);

Cantor, Fitzgerald has acted as principal broker for D-Z in its purchases of NJB shares (A346, 352);

Cantor, Fitzgerald is being well rewarded for its efforts on behalf of D-Z by contract, it is receiving a $30,000 fee plus expenses and in addition 5 per cent of the net purchase price payable in respect of all shares purchased (Exh. B, A291-92).*

Cantor, Fitzgerald, even now, is represented in the litigation below by the same counsel as represents D-Z.**

In sum, the role of Cantor, Fitzgerald bears no relationship to that of the normal function of a broker-dealer who, in executing a customer's order for the purchase of a security, merely passively advances a margin loan. To the contrary, the evidence incontrovertibly establishes that Cantor, Fitzgerald has from the outset been a full-fledged participant in D-Z's plan to take over NJB by stock purchases financed 100% by borrowed money. Such a role by a broker-dealer constitutes a clear violation of § 7(c) of the 1934 Act and § 220.7 of Regulation T. See p. 42, *supra*. See also *In re Sutro Bros. & Co.*, 41 SEC 443, 456-

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* Moreover, apparently yet additional lucrative compensation will be received by Cantor, Fitzgerald if it is in fact successful in arranging financing for D-Z's takeover. By letter dated April 24, 1974 it is provided that Cantor, Fitzgerald is to receive a percentage of any funds received by D-Z which Cantor, Fitzgerald "assists in arranging" (Exh. E, A225). Although the record is unclear as to whether the letter was formally executed by D-Z, Miller of Cantor, Fitzgerald acknowledged that he expects Cantor, Fitzgerald to be paid if they arrange such financing (A1258-59, 1262).

** See Reply to Counterclaims on behalf of additional defendant Cantor, Fitzgerald & Co. Inc., dated August 30, 1974.

57 (1963); *In re Looper and Company,* 38 SEC 294 (1958); *In re Irish,* Exchange Act Release No. 7718, [1964-66] CCH Fed. Sec. L. Rep. ¶ 77,297 (October 5, 1965), *aff'd, Irish* v. *SEC,* 367 F.2d 637 (9th Cir. 1966), *cert. denied,* 386 U.S. 911 (1967). *Cf. Remar* v. *Clayton Securities Corp.,* 81 F. Supp. 1014 (D. Mass. 1949).* Acceptance of such illegal credit by D-Z constitutes a violation of Regulation X.

The case at bar well exemplifies the very vice that the margin regulations were designed to guard against—to wit, over-leveraged purchases of public securities utilizing a "thin" equity base with the grave danger that in the event of a downturn in price, large blocks of stock would be forced to be involuntarily dumped on the market, thus inexorably accelerating the rate of market decline.** See pp.

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* Moreover, D-Z's borrowing from the noteholders—which the noteholders were aware was to be coupled with "traditional" margin loans to provide 100% credit financing for D-Z's purchases (Exh. G, A137)—would appear to constitute an independent violation of Regulation G on the part of the noteholders and Regulation X on the part of D-Z. Regulation G prohibits persons in the ordinary course of their business from extending credit for more than 50% of the purchase price of a margin security where secured. During most of the relevant period, noteholders' loans themselves supplied more than 50% of the price of the NJB shares purchased by D-Z (Exh. C, A113; Exh. D, A123; Exh. E, A127; Exh. F, A130; Exh. A, A207) and, of course, when coupled with "traditional" margin loans, constituted 100% borrowings. The sole asset of D-Z is its NJB stock: thus, the position of the noteholders in effective control of D-Z—pursuant to the "Private Placement Memorandum", the D-Z shares controlled by Davis and Zimmerman were to be placed in escrow as collateral for re-payment of the notes (Exh. G, A139)—in substance gave them the security of D-Z's sole asset, the shares of NJB. The violation is compounded in that a number of noteholders proceeded in turn to re-borrow their investment from banks (A471-79, 497, 1439-40, 1574, 1645-47, 1715-16).

The Davis affidavit submitted below claims that the escrow agreement—although promised in the private placement memorandum—was never formally executed (A249). If true, such admission is a telling commentary on the truthfulness of D-Z's disclosure to the noteholders in the memorandum. See pp. 50-52, *infra.*

** In the case at bar, D-Z's purchases of NJB shares have been made at an average price of in excess of $6 per share—all borrowed. As of the writing of this brief, NJB's stock is quoted on the American Exchange at $4 per share.

37-38, *supra*. Moreover, in the case at bar the 50% borrowing ceiling set by the Federal Reserve Board has not been exceeded by D-Z only to some minor extent. Rather, D-Z is proceeding with virtually *no* equity base at all to borrow *100%* of the funds necessary for its purchases. Such 100% borrowing plan—intimately participated in by a broker-dealer—indisputably violates both the letter and the spirit of the margin regulations.

2. D-Z's unregistered offer of its $1,250,000 issue of 6% promissory notes violated the Securities Act of 1933.

It is undisputed that D-Z's offering of its $1,250,000 6% promissory note issue constituted an "offer to sell [a security]" under Section 5 of the 1933 Act and that this offering was not registered by D-Z. The sole question upon this appeal as to the legality of D-Z's note offering is whether such offering was exempt under Section 4(2) of the 1933 Act as a private placement of securities.

The case law has severely circumscribed the "private placement" doctrine. See, *e.g., SEC* v. *Ralston Purina Co.*, 346 U.S. 119 (1953); *SEC* v. *Continental Tobacco Co.*, 463 F.2d 137 (5th Cir. 1972). It is clear that the statutory exemption must be strictly construed against the party seeking to assert it (see, *e.g., SEC* v. *Continental Tobacco Co., supra,* at 155; *Lively* v. *Hirschfeld,* 440 F.2d 631, 633 (10th Cir. 1971)) and that the burden of proof rests squarely upon the party who claims the exemption. See, *e.g., SEC* v. *Ralston Purina Co., supra; Gilligan, Will & Co.* v. *SEC,* 267 F.2d 461, 466 (2d Cir.), *cert. denied,* 361 U.S. 896 (1959); *Hill York Corp.* v. *American International Franchises, Inc.,* 448 F.2d 680, 690 (5th Cir. 1971).* "No

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* As set forth in *SEC* v. *Continental Tobacco Co., supra*:

> Under the *Ralston Purina* standard it was necessary that Continental prove that there existed no practical need for the application of § 5 of the Securities Act of 1933 to its 1969-70 offering or that the public benefits to be derived from any application of the Act were too remote. Continental's proof had to be "explicit, exact, and not built on conclusory statements * * *."
>
> —463 F.2d at 156

particular numbers [of offerees] are prescribed. Anything from two to infinity may serve: perhaps even one * * *." *SEC* v. *Ralston Purina Co., supra,* at 125 n. 11. See also *Gilligan, Will & Co.* v. *SEC, supra,* at 461 (only four purchasers; "the Ralston Purina case clearly rejected a quantity limit on the construction of the statutory term"); *Hill York Corp.* v. *American International Franchises, Inc., supra,* at 691 ("the fact that there were only thirteen actual purchasers is of course irrelevant"). As noted in *Hill York*:

> Obviously, however, the more *offerees,* the more likelihood that the offering is public. (Emphasis added.)
>
> —448 F.2d at 688

It is the number of offerees—and not the number of actual purchasers—that is determinative. See, *e.g., SEC* v. *Continental Tobacco, supra; United States* v. *Custer Channel Wing Corp.,* 376 F.2d 675 (4th Cir. 1967), *cert. denied,* 389 U.S. 850 (1968); *United States* v. *Hill,* 298 F. Supp. 1221 (D. Conn. 1969); *SEC* v. *Royal Hawaiian Management Corp.,* [1966-67] CCH Fed. Sec. L. Rep. ¶ 91,982 (C.D. Cal. 1967).* And, as noted in *Continental Tobacco*:

> [t]he ultimate test, of course, is whether the particular class of persons affected need the protection of the Act.
>
> —463 F.2d at 158

As there summarized:

> Courts have cited four relevant factors as being helpful in determining whether an offering of securities is public or private:

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* The newly adopted Rule 146, 17 C.F.R. § 230.146, would use a number of 35 purchasers as a partial test for determining the availability of the exemption, but sets forth stringent additional requirements upon the issuer. D-Z has made no claim that it has complied with Rule 146, nor could it very well. First, the Rule was adopted effective June 10, 1974, after most of the note sales were made. Second, as detailed below, there can be no question that D-Z has not even come close to meeting the stringent requirements of Rule 146 such as with respect to the furnishing of financial information to proposed purchasers.

1. The number of offerees and their relationship to each other and to the issuer.
2. The number of units offered.
3. The size of the offering.
4. The manner of the offering.

—463 F.2d at 158

Applying these criteria, it is clear that the D-Z offering was indeed a "public offering".

Thus, as set forth by the Fifth Circuit in *Hill York* and reiterated in *Continental Tobacco*:

> [W]here the number of offerees is so limited that they may constitute a class of persons having such a privileged relationship with the issuer that their present knowledge and facilities for acquiring information about the issuer would make registration unnecessary for their protection [*e.g.*, "an offering to a select group of high executive officers of the issuer who know each other and of course have similar interests and knowledge of the offering"] then the exemption is available.
>
> —463 F.2d at 159

On the other hand, as the Fifth Circuit set forth:

> if the offering is being made to a diverse and unrelated group, *i.e.*, lawyers, grocers, plumbers, etc., then the offering would have the appearance of being a public offering.
>
> —463 F.2d at 159

In the case at bar, on the uncontradicted record, D-Z's offerees constituted just such a "diverse and unrelated group". Thus, the evidence establishes that in the first instance the offering was made to a group of Atlanta residents having in common little other than their mutual acquaintanceship with Zimmerman (A505-07, 877). The offerees—at least some of whom were apparently persons of means—included a dermatologist (A1299), a gynecologist (A470), an orthodontist (A472), a retired exterminator (A509), a linen supply man (A467), two partners in a belt manufacturing company (A463), and a man engaged

in the lead recovery business (A509).* Then when Zimmerman's efforts in Atlanta—based upon his 100-name personal telephone directory (A505-07)—flagged (A875-77), the promoters went far afield: to New York (A866), to Chicago (A874, 880), to the beachfront in Florida (A880-81). They solicited people to solicit other people—Spear, a lawyer in Chicago "who said he had people who might be interested" (A858, 880). They solicited a group of businessmen in New York's jewelry district (A858, 867-74). They solicited next-door neighbors (A861); friends of friends (A860). They solicited people who—to their knowledge—in turn went to banks to borrow the funds to purchase the D-Z notes (A477-79, 497, 1439-40, 1574, 1645-47, 1715-16). The conceded purpose of D-Z's promoters was to solicit a sufficient number of offerees—without limitation—to come up with sufficient purchasers to take the entire $1,250,000 issue in anticipated units of $50,000 each (A391-96, 398-403, 511). *They kept no records of the num-*

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* Even if the offerees were "sophisticated" people, it is well settled that they would still be entitled to the registration protections of the 1933 Act. For the Courts have repeatedly held that "sophistication" or general knowledgeability cannot serve as a substitute for actual knowledge of the operative facts concerning the issuer. See, *e.g.*, *Hill York Corp.* v. *American International Franchises, Inc.*, *supra*, at 690 ("the level of sophistication will not carry the point"); *United States* v. *Custer Channel Wing Corp.*, *supra*, at 678 ("'sophistication' is not a substitute for 'access to the kind of information which registration would disclose'"). In fact, D-Z's offerees were not terribly sophisticated: of the actual purchasers deposed, none had sought the advice of any independent attorney, any accountant or any investment adviser for guidance as to the merits of the investment (A1312-13, 1555-57, 1580, 1613-15, 1648-49, 1699, 1702-04). None questioned as to why his right to convert the promissory note to a new "package" of D-Z debt and stock—the economic *sine qua non* of the deal—was nowhere expressly provided in the legal documents drafted by D-Z (A1394-99, 1459-63, 1553-56, 1576-80, 1617-22, 1669-71). With one possible exception none noticed or was aware that, assuming such conversion, the noteholders—who, in a time of record-breaking interest rates, had placed their money with D-Z at 6%—would end up paying $1,250 for each share of the common stock of D-Z (Exh. G, A139) whereas Davis and Zimmerman had paid only $100 per share for precisely the same stock (A435-36, 1398-1403, 1474-77, 1567, 1635-37).

ber of persons being solicited (A505, 507, 854).* Their lawyers did not instruct them to keep any record of the number or identity of the persons being solicited (A507, 853-54). Then, when the going got rough, they were not proud: they were even willing to sell in smaller pieces—a $12,500 "private placement" note purchaser (Exh. B, A313). And—to their own knowledge (Exh. B, A212)—at least one of their purchasers proceeded with his own secondary distribution selling "participations" in his notes to two other persons (Exh. B, A212; A1496-1503).

In sum, the offerees of the D-Z $1,250,000 note issue are a far cry from a "select group of high executive officers of the issuer who know each other and of course have similar interests and knowledge of the offering." See *SEC* v. *Continental Tobacco Co., supra,* at 159.

Moreover, D-Z's note offering was likewise established by the evidence to be flagrantly deficient on the touchstone of the private offering exemption—*i.e.,* that the offerees have access to or are supplied with information equivalent to that which they would receive in a registration statement. See, *e.g., SEC* v. *Ralston Purina Co., supra,* at 125-126 (offering to executive personnel of an issuer might qualify for exemption because such persons would "have access to the same kind of information that the act would make available in the form of a registration statement"); *Hill York Corp.* v. *American International Franchises, Inc.,* 448 F.2d 680, 689 (5th Cir. 1971) ("every offeree had to have information equivalent to that which

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* *Cf. SEC* v. *Ralston Purina Co., supra,* at 121 ("No records were kept of those to whom the offers were made"). Since the burden of proof rests with the party seeking to claim the exemption, the courts have held that an offering will be deemed to be a public offering absent an affirmative showing *by the claimant* as to the nature and number of the offerees. See, *e.g., SEC* v. *Continental Tobacco Co.,* 463 F.2d 137, 161 (5th Cir. 1972); *Hill York Corp.* v. *American International Franchises, Inc.,* 448 F.2d 680, 691 (5th Cir. 1971); *Repass* v. *Rees,* 174 F. Supp. 898, 904 (D. Colo. 1959). Here, as in *Strahan* v. *Pedroni,* 387 F.2d 730, 731 (5th Cir. 1967), the evidence establishes that "the offer to sell such [securities] was in fact intended * * * to be open to any person having the required purchase price."

a registration statement would disclose''); *United States* v. *Custer Channel Wing Corp.*, 376 F.2d 675, 678 (4th Cir. 1967), *cert. denied*, 389 U.S. 850 (1968) (''A purchaser of unregistered stock must be shown to have been in a position to acquire similar information [to the categories of information required to be included in a registration statement] about the issuer.''); *Lively* v. *Hirschfeld*, 440 F.2d 631, 633 (10th Cir. 1971); Rule 146(e)(1). Thus, the uncontradicted evidence establishes:

> that no financial statement or other financial information whatsoever regarding the issuer, D-Z, was furnished to any offeree (A501-02, 1391, 1475-76, 1567-68, 1639, 1714);
>
> that—although virtually the sole asset of D-Z consisted of the stock of NJB (A846) and the sole purpose for which it was formed was to acquire NJB (A377, 1279-81) (so that in essence the note purchasers were investing in the stock of NJB, *cf.* SEC Rule 140)—no financial statement or other financial information whatsoever regarding *NJB* was furnished to the offerees (A499-501, 1392, 1475, 1540, 1572, 1639, 1714);
>
> that D-Z did not even disclose the *identity* of NJB to most of the offerees (Exh. G, A135; A491, 498, 1344-45, 1520-21, 1615, 1628-29);
>
> that, to the contrary, D-Z concededly affirmatively and intentionally *withheld* the identity of NJB as the target company from the offerees (Exh. G, A135; A491, 498, 1330-31, 1337, 1344, 1559-62, 1628-29)—thus depriving the offerees even of public information with respect to NJB that would otherwise have been available to them, *i.e.*, D-Z affirmatively *denied* the offerees ''access'' to such crucial information;
>
> that, according to the actual terms of the ''private placement memorandum'' and the noteholders' agreements, the investors—at a time of record-breaking interest rates—were receiving for their money solely a 6% promissory note in a shell corporation: the documents prepared by D-Z are silent as to the very essence of the note offering, the ''contemplated'' right to convert a note into a new \$50,000 note-equity ''unit'' to consist of 4 shares of D-Z's common stock and a new 6% two-year \$45,000 promissory note (Exh. G, A138-40; A446);

that the "private placement memorandum" fails to disclose that whereas—if the noteholders should ever indeed be offered that "privilege" of converting $5,000 of their investment into equity—they would be paying $1,250 per share for the same stock for which Messrs. Davis and Zimmerman had paid only $100 per share (Exh. G, A139; A435-36, 1398-1403, 1474-77).

In sum, the record in this case presents a classic example of an offering of securities in which the protections that would be afforded by a registration statement have not been fulfilled. On the conceded and undisputed evidence, D-Z could not remotely meet its burden of satisfying the stringent requirements of the private offering exemption. D-Z's unregistered offering of its $1,250,000 6% promissory note issue indisputably violated the 1933 Act.*

3. *D-Z is an unregistered investment company under the Investment Company Act of 1940.*

The fact of D-Z's public offering of its securities is also determinative of D-Z's illegal status under the 1940 Act. Thus, not only does D-Z—by its very name "D-Z Investment Company"—"hold itself out" to be an investment company, Section 3(a)(1), but it is also an investment company under Section 3(a)(3) in that virtually its sole asset—its 13% holding of the outstanding shares of NJB—constitute investment securities under Section 2(a)(36) of the 1940 Act. Therefore, unless exempt, D-Z has been required to register under the 1940 Act as an investment company. The sole conceivable exemption would be that provided by Section 3(c)(1) of the Act**; that exemption, however, is inapplicable in that—as has been detailed above—D-Z has made a public offering of its securities.

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* As previously noted, D-Z itself in its brief to the District Court did not even attempt to contest the trustees' showing of illegality. See Plaintiff's Memorandum, p. 42.

** "Any issuer whose outstanding securities (other than short-term paper) are beneficially owned by not more than 100 persons *and which is not making and does not presently propose to make a public offering of its securities*". (Emphasis added.)

D-Z concededly has not registered with the SEC as an investment company and is in violation of the Act. Accordingly, the Act, Sections 7 and 47, makes "void" *all* contracts entered into by D-Z—its sale of its promissory notes and its very purchases of NJB stock alike.

* * *

Thus, from beginning to end, D-Z's scheme for financing its take over of NJB has constituted a parade of illegalities. Starting with a $10,000 equity shoestring, D-Z has set out to borrow all of the remaining funds needed for the take over; has done so with reckless disregard for the prohibitions and requirements of the margin regulations and securities laws; has planned ultimately to raid the assets of the target company itself to re-pay the illegal borrowings. And, by false and misleading 13Ds, D-Z has concealed the true facts from the investing public. The District Court's decision would permit D-Z to continue its illegal scheme with impunity. The District Court's decision must be reversed.

POINT IV

D-Z and its investment banker have engaged in an unlawful solicitation of proxies from the shareholders of NJB. The trustees have clear standing to raise such illegality and an injunction must issue.

A. The unlawful D-Z proxy solicitation.

The trustees in the court below established that—after D-Z was rebuffed by Judge Cannella and this Court in its attempt to delay the June 13 regular annual meeting of stockholders of NJB (A20-25, 75-76)—D-Z proceeded to engage in an illegal proxy solicitation by telephoning NJB shareholders to seek their consents for the call of a special meeting of shareholders.*

* Under the NJB Declaration of Trust, the consent of 20% of the outstanding shares is required for the call of such special meeting (A84). D-Z itself at the time in question had accumulated approximately 9.5% (Exh. C, A115; Exh. A, A207).

The District Court in its opinion held that the trustees' position was "without any support in fact" (A365). It is respectfully submitted that on the record before it, such conclusion of the District Court is inexplicable and that the incontrovertible evidence of the illegal proxy solicitation was in fact established by the *admissions* of the very Cantor, Fitzgerald personnel involved.

Thus, uncontradicted evidence adduced by the trustees shows that William Schwartz, a vice president of Cantor, Fitzgerald, D-Z's investment banker—commencing the very day after the June 13 annual meeting and utilizing summary lists of major holders of NJB's shares prepared by Cantor, Fitzgerald from the NJB shareholders list (Exhs. K, L, A231-38; A1169-71)*—proceeded to place telephone calls to such major shareholders on behalf of D-Z (A1023-1154).

It is conceded by Schwartz that by such telephone calls he reached *29* such major shareholders (A1023-1154).** The documentary evidence establishes that those 29 shareholders held of record 120,759 shares or approximately 9.5% of the total outstanding shares of NJB (Exh. A, A207; Exhs. K, L, A231-38).*** The uncontradicted evidence further shows that prior to the commencement of the Schwartz telephone calls, William Miller, a senior vice

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* The misuse of the NJB shareholders list by D-Z is particularly egregious. The list was furnished to D-Z by NJB pursuant to an order of a Massachusetts court (A1168). It is clear that the list was ordered to be supplied for D-Z's legitimate use in connection with the NJB annual meeting. It was manifestly not contemplated that the list would be used to facilitate D-Z's unlawful solicitation of consents to a special meeting, nor was it to be used as the springboard for Cantor, Fitzgerald's attempt to purchase blocks of NJB stock through telephone solicitations of major shareholders.

** And Schwartz by his own testimony attempted unsuccessfully to reach many more large block shareholders of NJB (*e.g.*, A1044-45, 1083-86, 1098-99, 1140, 1145).

*** In fact, the percentage of total NJB shares represented by recipients of the Schwartz telephone calls is still greater in view of the family or other related holdings of many of those called.

president of Cantor, Fitzgerald, had supplied Schwartz with the summary lists (A1179-80) and told Schwartz to contact the holders of NJB stock in an attempt to purchase their shares (A1007). Miller further explained to Schwartz that a special meeting of the NJB shareholders could be convened at the request of 20% or more of the NJB shareholders and that D-Z was desirous of convening such a special meeting for the purpose of ousting existing NJB management (A1184). Schwartz proceeded to place telephone calls in which he sought alternatively to purchase the shareholders' stock or to enlist support for the call of a special meeting (*e.g.*, A1110-13, 1118-21, 1123-25, 1127-32). Then Miller gave Schwartz new instructions: to desist from attempts to purchase more shares, but to continue to contact shareholders (A1017-18, 1182-83).

As to 13 of the telephone conversations that Schwartz concededly had with major shareholders of NJB (Exhs. K, L, A231, 238; A1026-1154), Schwartz' own testimony establishes that Schwartz had explicit discussions with the shareholders concerning a possible special shareholders meeting and the shareholders' positions with respect thereto (A1064, 1073-75, 1087, 1090-93, 1095-97, 1103, 1107-09, 1112-13, 1118-21, 1123-25, 1128-30, 1132, 1141-42, 1144, 1146-47, 1151-53).* It is clear that the Schwartz calls constituted a proxy solicitation.

The argument made by D-Z below—and apparently accepted by the District Court (A365)—that the Schwartz telephone calls were merely an attempt to "test the waters" is not remotely supported by the record evidence. Rather on Schwartz' own testimony in his telephone calls—after identifying himself as being affiliated with Cantor, Fitzgerald—he advised the recipient of the call that he represented a large NJB shareholder who was dissatis-

* As to the remaining 16 calls which Schwartz sought to characterize as being primarily designed to purchase the shareholders' stock, Schwartz nonetheless admits that in his conversations he did not confine himself to the subject of purchasing stock but also sought "to ascertain the attitude of people toward the management" (A1063, 1115).

fied with the NJB management and wished to call a special shareholders meeting to oust management; he "might have" asked whether the shareholder "would join in an effort to obtain a special meeting." (A1077; see also A1075, 1097, 1103, 1108, 1112, 1119, 1125, 1131-32, 1141-42). (The accounts of recipients of the Schwartz telephone solicitations are even more explicit: Schwartz advised that he represented a "proxy group"; Schwartz requested the shareholders to join with Schwartz' client in an effort to change management (A166-70)). Moreover, the documentary evidence of Schwartz' own contemporaneous handwritten notations on the summary stockholders list used by him to make the calls contains next to the names of individual shareholders reached by him such candid notations as "will not join in", "may give proxy" and "will give proxy" (Exh. L, A236, 238). Such notations leave no room for doubt as to the nature of Schwartz' solicitation.

It is undisputed that D-Z has not purported to comply with the SEC's proxy rules: that no proxy material has been filed with the SEC; that no proxy statement was furnished to any of the shareholders solicited. It is further undisputed that NJB stock is within the proxy rules and that more than the statutory minimum of ten shareholders were contacted.

It is submitted that under settled principles of law, the telephone solicitation campaign conducted by Cantor, Fitzgerald on behalf of D-Z constitutes an illegal proxy solicitation within the meaning of Section 14(a) of the 1934 Act and the proxy rules promulgated thereunder.

"Proxy" under both Section 14(a) of the 1934 Act and Rule 14a-1(d) includes "every proxy, consent or authorization". "Solicit" and "solicitation" are broadly defined by Rule 14a-1(f) to include:

(1) *any request for a proxy* whether or not accompanied by or included in a form of proxy;

(2) any request to execute or not to execute, or to revoke, a proxy; or

(3) the furnishing of a form of proxy *or other communication to security holders under circumstances*

> *reasonably calculated to result in the procurement* withholding or revocation *of a proxy.* (Emphasis added.)

As this Court has pointed out in *Studebaker Corp.* v. *Gittlin,* 360 F.2d 692, 695 (2d Cir. 1966), the proxy rules contain definitions which "exhaust the sweep of the power * * * conferred" upon the SEC under Section 14(a) of the Exchange Act.

It is clear that a "solicitation" can be made orally. See, *e.g.,* Rule 14a-9; Sec. Exch. Act Rel. No. 3347 (1942) 1; 2 Loss, *Securities Regulation* 874 (2d ed. 1961); 11A Gadsby, *Business Organizations* § 7.02 (1970). Under the SEC's Rules, no solicitation may be made unless the person solicited has previously or is concurrently furnished with a written proxy statement. Rule 14a-3(a). Such proxy material must be previously filed with the SEC. Rule 14a-6.

It is submitted that there can be no dispute that the Schwartz telephone calls constituted an impermissible "solicitation" of a "proxy, consent or authorization". It is well settled that the terms "proxy, consent or authorization" as used in the proxy rules are to be broadly construed. Thus, as set forth in *Greater Iowa Corp.* v. *McLendon,* 378 F.2d 783, 796 (8th Cir. 1967):

> While "proxy" is perhaps a narrow word of art implying an agency relationship, the statute goes further. *The words "consent" and "authorization" are extremely broad words and are not limited by the word "proxy."* No doubt Congress intended that the words of the Act be given the broadest meaning necessary to effectuate its stated purposes. SEC v. Joiner Leasing Corporation, [320 U.S. 344, 350-351 (1943)]. By including all of these words in the disjunctive, we believe *Congress intended to cover the entire field of solicitation for corporate control and all of the various solicitation situations which might arise from time to time, whether conventional, novel, irregular or unorthodox.* (Emphasis added.)

In *Dunning* v. *Rafton,* [1964-66] CCH Fed. Sec. L. Rep. ¶ 91,660 (N.D. Cal. 1965), the court similarly held that the

term "consent" is not limited by the term "proxy" and that solicitation of "consents" would include circularizations requesting or urging a shareholder to concur in the solicitor's proposal:

> The Court finds upon examination of the purpose of the Act that it should accept the meaning of "consent" as it is generally understood and not restrict it to the same meaning as the word "proxy". The purpose of the Securities Exchange Act and the rules and regulations promulgated thereunder, was to protect the investing public from misleading statements made in the course of a struggle for corporate control. *Securities and Exchange Commission* v. *May,* 229 F.2d 123 (2d Cir. 1956). ***Whether this struggle involves solicitation for someone else's proxy or circularizations urging him to vote, himself, in a certain manner, does not lessen the need for protection against misleading statements.*** Were the word "consent" limited in meaning to that of conferring authority upon another, an easy way would be open to circumvent the statute; one need only arrange for the voting for corporate matters directly by the shareholders, rather than by proxy at shareholders' meetings, and the way would be open to the spread of misinformation. (Emphasis added.)
>
> —[1964-66] CCH Fed. Sec. L. Rep. ¶ 91,660 at 95,437

As to the meaning of "solicitation", this Court in the leading case of *SEC* v. *Okin,* 132 F.2d 784, 786 (2d Cir. 1943), set forth the now accepted general rule that the "solicitation" of a proxy includes any communication to shareholders which is "part of a continuous plan ending in solicitation and which prepare[s] the way for its success." In *Studebaker Corp.* v. *Gittlin, supra,* this Court reemphasized the rule of *SEC* v. *Okin,* holding that a circularization of stockholders to obtain authorization to inspect the stockholders list preparatory to the solicitation of proxies was a step in a proxy contest* and thus constituted a

* It is clear that even if the Schwartz telephone calls were—as claimed by D-Z—only an attempt to D-Z to determine the NJB shareholders' "attitude towards management"—the D-Z telephone canvass was a step in a proxy contest and thus a "solicitation" under the ***Okin*** and ***Gittlin*** cases.

"solicitation":

> Presumably the stockholders who gave authorizations were told something and, as Judge L. Hand said in *Okin,* "one need only spread the misinformation adequately before beginning to solicit, and the Commission would be powerless to protect shareholders." 132 F.2d at 786. Moreover, the very fact that a copy of the stockholders list is a valuable instrument to a person seeking to gain control, see fn. 1, is a good reason for insuring that shareholders have full information before they aid its procurement. We see no reason why, in such a case, the words of the Act should be denied their literal meaning.
>
> —360 F.2d at 696

Moreover, in order for a communication to be a "solicitation" it is not necessary that the communication request any inaction or action by the recipient. *Sargent* v. *Genesco, Inc.*, [Current] CCH Fed. Sec. L. Rep. ¶ 94,496 at 95,743 (5th Cir. 1974); Sec. Exch. Act Rel. No. 5276 (1956). Indeed, a "solicitation" has been held to include a communication with shareholders which contained an express statement that proxies were not being solicited. *Suburban Electric Securities Co.*, 23 SEC 5, 11 fn. 11 (1946).

Thus, on the conceded facts and applying settled principles of law there can be no doubt that an illegal proxy solicitation indisputably occurred. The District Court's opinion—which is barren of a single citation to any of the controlling authorities from this or any other court—that the trustees' position was "without any support in fact" is plainly in error.

B. An injunction must issue by virtue of D-Z's violations of the proxy rules.

There can be no question that a target company has standing to assert violations of the proxy solicitation rules by a company attempting a takeover bid. *E.g., Studebaker Corp.* v. *Gittlin, supra,* at 694-95; *GAF Corporation* v. *Milstein, supra* at 719. As this Court has noted in *Gittlin:*

> [T]he legislative history shows that Congress anticipated protection from "irresponsible outsiders seek-

> ing to wrest control of a corporation away from honest and conscientious corporation officials," S.Rep. No. 1455, 73d Cong., 2d Sess. 77 (1934), quoted in 2 Loss, supra at 950, and the Proxy Rules are shot through with provisions recognizing that in contests for control the management has a role to play as such and not merely insofar as the managers are stockholders. Moreover, it is common knowledge that a contest for control may be only the prelude to an arguably damaging transaction to be carried out by the winner with the aid of the corporate proxy machinery or even without further stockholder vote.
>
> —360 F.2d at 695

And, it is clear that D-Z's violations of the proxy rules can in no way be dismissed as *de minimis*. Rather, as shown, D-Z—itself then the holder of close to 10% of the shares—proceeded to solicit block shareholders of NJB representing an additional 10%. As Judge Learned Hand set forth in *Okin*, it is critical that the coverage of the proxy rules extend to the preliminary stages of proxy solicitation, for,

> were it not so, an easy way would be open to circumvent the statute; one need only spread the misinformation adequately before beginning to solicit, and the Commission would be powerless to protect shareholders. The earlier stages in the execution of such a continuous purpose must be subject to regulation, if the purpose of Congress is to be fully carried out.
>
> —132 F.2d at 786

Moreover, the importance of the entry of effective relief to neutralize proxy violations and to prevent future violations has been emphasized repeatedly by the Supreme Court. In *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 386 (1970), the Court reemphasized its landmark holding in *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964), stating:

> We held in *Borak* that upon finding a violation the courts were "to be alert to provide such remedies as are necessary to make effective the congressional purpose," noting specifically that such remedies are not to be limited to prospective relief. 377 U.S., at 433, 434, 84 S. Ct. at 1560.

By virtue of these controlling authorities, an injunction must issue to neutralize D-Z's clearly demonstrated violations of the proxy rules and to restrain D-Z from future violations.

POINT V

D-Z has engaged in an unlawful tender offer for control of NJB in violation of the tender offer provisions of the Williams Act.

A. D-Z's program of open market and privately negotiated purchases of NJB stock constitutes an unlawful tender offer for control of NJB.

In the case at bar, no "conventional" formal tender offer has yet been made by D-Z. It is nonetheless the position of the trustees that, under a proper reading of Section 14(d) and (e) of the 1934 Act, the totality of conduct by D-Z—massive purchases of NJB shares both on-the-market and by private solicitation off-the-market pursuant to an unswerving intention to obtain control through stock purchases—constitutes in contemplation of law a "tender offer" within the meaning of the Williams Act.

The District Court disagreed. The District Court held as a matter of law that "open market purchases cannot be a 'tender offer'" (A363). The District Court further held that D-Z's other activities did not "amount to a 'tender offer'" (A364).

It is submitted that the District Court erred; that the courts and authorities that have most recently viewed the congressional purpose and intent in enacting Section 14(d) and (e), have concluded that the statutory protection to shareholders is not limited to the circumstance of a "conventional" tender offer, but includes any case where the totality of the acquiring company's conduct has the equivalent "shareholder impact" of such a "conventional" tender offer.

The Williams Act added new Sub-sections 14(d) and (e) to the 1934 Act as remedial legislation in the corporate takeover context. Basically, these sections and the rules promulgated by the SEC pursuant thereto require that if a "tender offer" is being made for more than 5% of the stock of a subject corporation: a specified filing must first be made with the SEC; an offering circular complying with the SEC's requisites must be furnished to each shareholder; and parity of treatment must be afforded all shareholders. See Section 14(d); Rule 14d-1.

Neither Congress in drafting the Williams Act, nor the SEC in adopting implementing rules, has defined the term "tender offer." Nonetheless, it is clear from the legislative history of the Act that it was not intended to be restricted to "conventional" tender offers but rather was meant to encompass all methods of takeovers sought to be achieved by large-scale stock purchase programs. In *Cattlemen's Investment Co. v. Fears,* 343 F. Supp. 1248 (W.D. Okla.), *vacated per stipulation,* Civil No. 72-152 (1972) the court was faced with the precise question of whether a Williams Act "tender offer" could exist in the absence of a "conventional" tender offer. The court answered in the affirmative holding that the purpose of the Williams Act

> is to provide investors who hold equity interests in public corporations, material information with respect to the potential impact of any effort to acquire control of a company, sufficient time within which to make an unhurried investment decision as to whether to dispose of or retain their securities, and to assure fair treatment of the investors. We deem it abundantly clear that there is an obligation on persons attempting to gain control of a corporation by means of tender offers to make the required filings and disclosures.
>
> —343 F. Supp. at 1251

The court went on to hold that the defendants' telephonic, mail and in-person solicitations of various of the target company's shareholders constituted a "tender offer", stating:

> [A]n active and widespread solicitation of public shareholders in person, over the telephone and through

> the mails, contain potential dangers which Section 14[d] of the statute is intended to alleviate. The defendant, in not complying with the statute, deprived shareholders of information prescribed by the Rule, which information was material to their investment decisions, and denied to them the fair treatment provided by other parts of Section 14[d]. In truth, the contacts utilized by the defendant seem even more designed than a general newspaper advertisement, the more conventional type of "tender offer", to force a shareholder into making a hurried investment decision without access to information, in circumvention of the statutory purpose. * * * When we consider the plain language of the statute and rules and the purposes to be served, we have no hesitancy in concluding that the activities of the defendant in making contact with plaintiff's shareholders by the use of the mails, telephone calls, and personal visits, for the purpose of purchasing their shares, constitute "tender offers for, or a request or invitation for tender offers of" their stock within the meaning of the statute.
>
> —343 F. Supp. at 1251-52

Accord, Cattlemen's Investment Co., [1971-72] CCH Fed. Sec. L. Rep. ¶ 78,775 (1972). See *LSL Corporation*, [1973-74] CCH Fed. Sec. L. Rep. ¶ 79,715 (1974) (abandonment by SEC staff of previous view expressed in *American General Ins. Co.*, [1971-72] CCH Fed. Sec. L. Rep. ¶ 78,588 (1971) that open market purchases did not constitute a tender offer). See also *Smallwood* v. *Pearl Brewing Co.*, 489 F.2d 579, 596-99 (5th Cir. 1974).

In *Nachman Corp.* v. *Halfred, Inc.*, [1973-74] CCH Fed. Sec. L. Rep. ¶ 94,455 (N.D. Ill. 1973), Judge McLaren of the Northern District of Illinois—albeit finding no "tender offer" to have occurred on the particular facts before him—nevertheless again recognized that a Williams Act "tender offer" was not confined to a "conventional" tender offer. Rather, the court expressly adopted the "shareholder impact" test as reflected in the analysis and conclusions of an extensive Harvard Law Review Note, *The Developing Meaning of "Tender Offer" Under the Securities Exchange Act of 1934,* 86 Harv. L. Rev. 1250 (1973) (the "*Harvard Note*") in reaching its determination

> that the definition of ["tender offer"] should extend beyond ... conventional meaning to offers likely to pressure shareholders into making uninformed, ill-considered decisions to sell, *i.e., offers with the same impact as the conventional tender offer.* (Emphasis added.)
>
> —[1973-74] CCH Fed. Sec. L. Rep. ¶ 94,455 at 95,590

As was recognized in the *Harvard Note,* in the ordinary market purchase the shareholder comes forward to sell on his own, *i.e.,* his individual decision to dispose of his stock is not influenced by the anonymous purchaser. If, however, privately negotiated or open market purchases are made at a time when it is public information that the purchaser is conducting a cash buying program for a percentage of the target's shares in an effort to acquire a control position in that target, the characterization of the purchase program as a tender offer would flow from the "shareholder-impact" test. See *Havard Note, supra,* at 1279. See also Lipton, *Book Review,* 72 Mich. L. Rev. 358, 362-67 (1973); Note, *The Scope of Section 14(d): What is a Tender Offer?,* 34 Ohio St. L.J. 375, 382 (1973); Griffin & Tucker, *The Williams Act, Public Law 90-439—Growing Pains? Some Interpretations with Respect to the Williams Act,* 16 Howard L.J. 654 (1971).

Quite recently, the Northern District of Illinois again had the "non-conventional" tender offer question before it. See *Loews Corp.* v. *Accident & Casualty Ins. Co.,* 74 C. 1396 (N.D. Ill.) (bench opinion, July 11, 1974; findings of fact, conclusions of law and order, Aug. 20, 1974) (Marshall, J.). There *all* of the purchases in question had taken place on the open market. The court—applying the "shareholder impact" test—held that such open market purchases coupled with a publicized intent to acquire a specified percentage of the subject company's shares constituted a "tender offer" within the protections of the Williams Act. A preliminary injunction issued.

The evidence is uncontradicted that D-Z has been acting pursuant to an unswerving plan to acquire control of NJB (Exh. A, A108-09; Exh. B, A110; Exh. A, A113-15; Exh.

B, A211; Exh. C, A213-20; Exh. D, A221-24; A762, 777) and that D-Z was in fact formed for this very purpose (A377, 1279-81). D-Z's takeover plans have been well publicized in both the general and financial press (Exhs. F-J, A226-30). D-Z has in fact—when the requisite financing appeared at hand—formulated specific plans to acquire control of NJB by a "conventional" tender offer (A599-606, 765-77; Exh. D, A221-24). Indeed, express letters of agreement toward this purpose were entered into (Exh. A, A108-09; Exh. C, A213-20) only to be abandoned when the anticipated financing aborted. In each case, D-Z then fell back upon a stock "accumulation" program in order to obtain control (A774-78, 646-51, 573-74). D-Z's stock "accumulation" program has consisted of the placing of unlimited quantity stock purchase orders upon the market (A570, 573-74, 649) coupled with an intensive campaign of off-the-market direct personal solicitations of shareholders to attempt to buy their stock (A690-95, 1026-1154, 1175-76). This stock "accumulation" program has resulted in D-Z over a short period of time acquiring approximately 13% of the total outstanding stock of NJB (Exh. B, A312; Exh. C, A115).

It is submitted that the totality of D-Z's conduct herein has inevitably had the "shareholder impact" that has been recognized by the courts in *Cattlemen's, Nachman* and *Loews* as triggering the "tender offer" protections of the Williams Act. NJB shareholders have been, and continue to be, pressured to consider the desirability of selling their NJB positions while D-Z remains a willing buyer. Yet NJB shareholders are being forced to act without any of the protections designed for them by Congress in such a circumstance.

Appellants submit that D-Z is, as a matter of law, engaged in a tender offer.

B. The trustees have clear standing to raise D-Z's violations of the tender offer provisions of the Williams Act.

Once again, the law is clear that the target of an illegal tender offer has standing to raise the acquiror's Williams Act violations. *E.g., Gulf & Western Industries Inc.* v.

Great Atlantic & Pacific Tea Co., 476 F.2d 687, 696 (2d Cir. 1973); *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 944-46 (2d Cir. 1969). Indeed, this Court in *Gulf & Western* emphasized that in so acting the target company "is assuming a dual role, including that of a private attorney general" to protect the public interest. 476 F.2d at 699. An injunction must enter to bar D-Z's continuing illegal purchases.

Summary

Davis and Zimmerman concocted a scheme. They would invest $10,000 in equity in an empty corporate vessel. They would then use this corporate shell to attempt to takeover control of a major listed REIT, the underlying assets of which were worth more than the present-day market price of its shares. They would have their corporate shell borrow 100% of the funds necessary for the takeover. They would conceal the true facts of their scheme from the public. Ultimately, after achieving control, they would destroy the trust's REIT status and use the trust's own assets to re-pay the borrowings.

In furtherance of this scheme, their corporate vehicle D-Z has done everything that an acquiring company could possibly do other than make a formal tender offer. It has publicized its takeover bid; it has entered unlimited purchase orders upon the American Stock Exchange; it has actively solicited purchase of shareholders' blocks off-the-Exchange; it has conducted a telephone campaign to solicit other major shareholders to join with it in its takeover plan. It has done all this:

> having filed a Schedule [illegible] and amendments that conceal its own "shell" corporation status and are egregiously false and misleading as to its source of funds and plans for the trust (including its plan to destroy the trust's REIT status and use the trust's assets to re-pay D-Z's own borrowings) (Point II);
>
> with but $10,000 of equity and using 100% borrowed funds illegally raised in contravention of the securities laws and margin regulations (Point III);
>
> without compliance with the proxy rules (Point IV);
>
> without compliance with the tender offer requirements of the Williams Act (Point V).

The District Court's opinion would nonetheless leave D-Z free to continue its illegal scheme without hindrance.

As this Court has repeatedly emphasized, in cases such as this, it is not only the interest of the target company but the public interest as well that must be protected. See *GAF Corp.* v. *Milstein*, *supra*, 453 F.2d at 717-20; *Gulf & Western Industries, Inc.* v. *Great Atlantic & Pacific Tea Co.*, *supra*, 476 F.2d at 698-99. See also *Mosinee Paper Corp.* v. *Rondeau* [Current], CCH Fed. Sec. L. Rep. ¶ 94,719 at 96,374-75 (7th Cir. July 16, 1974); *Bath Industries, Inc.* v. *Blot*, 427 F.2d 97, 113 (7th Cir. 1970); *General Host Corporation* v. *Triumph American, Inc.*, 359 F. Supp. 749, 759 (S.D.N.Y. 1973). Yet as this brief is written "investors in general as well as the stockholders of [NJB]"—the members of the public sought to be protected by the disclosure provisions of the Williams Act—are every day being forced to make the investment decision to buy, sell or hold NJB shares without the protection of truthful disclosure by D-Z; without the information to which they are entitled by law in order properly to "assess the potential for changes in corporate control and [to] adequately evaluate the company's worth". See *GAF Corp.* v. *Milstein*, *supra*, 453 F.2d at 717; *Bath Industries, Inc.* v. *Blot*, *supra*, 427 F.2d at 109.

As this Court has likewise made clear, in the takeover context the optimum point in time for granting effective relief is upon a motion for a preliminary injunction. As stated in *Electronic Specialty Co.* v. *International Controls Corp.*, *supra*, 409 F.2d at 947:

> [T]he application for a preliminary injunction is the time when relief can best be given. * * * [W]e think that in administering § 14(d) and (e), district judges would do well to ponder whether, if a violation has been sufficiently proved on an application for a temporary injunction, the opportunity for doing equity is not considerably better than it will be later on.

Accord, *Sonesta International Hotels Corp.* v. *Wellington Associates*, 483 F.2d 247, 250 (2d Cir. 1973) once a takeover has been accomplished "it becomes difficult, and sometimes virtually impossible, for a court to 'unscramble the

eggs'"); see also *Missouri Portland Cement Co.* v. *Cargill, Inc.,* [1973-74] CCH Fed. Sec. L. Rep. ¶ 94,595 at 96,095-23 (2d Cir. June 10, 1974) (in Williams Act cases, preliminary injunction causes no undue hardship to acquiring company as "where needed correction could speedily be made"; rule different in antitrust cases where "the temporary injunction will continue in force until the trial and decision of a complicated antitrust case before a busy district judge").

Finally, as this Court set forth in *Gulf & Western Industries, Inc.* v. *Great Atlantic & Pacific Tea Co., supra,* 476 F.2d at 699.

> [D]oubts as to whether an injunction sought is necessary to safeguard the public interest—when the public interest involved is as clear, pervasive and vital as the record here demonstrates—should be resolved in favor of granting the injunction.

In the case at bar, it is submitted that there are no "doubts". Viewed individually, each of the major violations of law committed by D-Z in the course of its take-over attempt requires the issuance of injunctive relief. Viewed cumulatively, any conceivable possibility of doubt vanishes.

CONCLUSION

The order of the District Court denying a preliminary injunction should be reversed and the injunction directed to issue.

Respectfully submitted,

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[redacted] Service of Two copies of the within Brief is hereby admitted this 16th day of September 1971

....
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5:08 P.M.

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